## OFFICIAL STATEMENT

# $713,480,000
# Puerto Rico Public Buildings Authority

Consisting of

**$128,895,000 Revenue Refunding Bonds, Series L**

**$584,585,000 Public Education and Health Facilities Refunding Bonds, Series M**

## Guaranteed by the Commonwealth of Puerto Rico

Dated June 1, 1993† Due July 1, as shown on the inside cover

The Bonds will be issued in fully registered form and when issued, will be initially registered in the name of Cede & Co., as nominee of The Depository Trust Company, which will act as depository for the Bonds. See "Book-Entry Only System" under *Description of the Bonds.*

A portion of the Bonds will be delivered as Tax Exempt Components (the "TXCs") and Indexed Inverse Floaters (the "Indexed Inverse Floaters"). See "TXCs" and "Indexed Inverse Floaters" under *Description of the Bonds* and Appendices VI and VII attached hereto. The Bonds will be issued in denominations of $5,000 or any multiple thereof, except in the case of the Indexed Inverse Floaters which will be issued in denominations of $100,000 and any multiple thereof until the Scheduled Conversion Date or Optional Conversion Date, and the TXCs which will be issued in denominations of $5,000 principal amount or Notional Principal Amount (as defined herein), or any multiple thereof.

Interest on the Bonds will be payable January 1, 1994 and each January 1 and July 1 thereafter. Interest on the Indexed Inverse Floaters will accrue from the date of initial delivery through the day prior to the Scheduled Conversion Date indicated on the inside cover page hereof at the Indexed Inverse Floaters Rate and thereafter at the Base Rate. Owners of the Indexed Inverse Floaters may elect, subject to certain conditions, on any Business Day prior to the Scheduled Conversion Date to convert the interest on not less than $5,000,000 principal amount of the Indexed Inverse Floaters of the same maturity to the Converted Rate. See Appendix VII attached hereto. Payment on the TXCs will be made in the manner described in Appendix VI attached hereto.

**The Bonds will be subject to redemption as described herein.**

**The Revenue Refunding Bonds, Series L, the $133,594,258 outstanding Revenue Bonds (calculated by excluding all interest accretion on capital appreciation bonds and excluding the outstanding Revenue Bonds to be refunded) and any additional Revenue Bonds issued under the 1970 Bond Resolution, will be secured equally and ratably by a pledge of the rentals of office buildings leased by the Authority to departments, agencies and instrumentalities of the Commonwealth. The good faith and credit of the Commonwealth are pledged to the payment or advance of all such rentals.**

**The Public Education and Health Facilities Refunding Bonds, Series M, the $344,924,711 outstanding Public Education and Health Facilities Bonds (calculated by excluding all interest accretion on capital appreciation bonds and excluding the outstanding Public Education and Health Facilities Bonds to be refunded) and any additional Public Education and Health Facilities Bonds issued under the 1978 Bond Resolution, will be secured equally and ratably by a pledge of the rentals of public education and health facilities leased by the Authority to the Commonwealth's Department of Education and Department of Health, respectively. The good faith and credit of the Commonwealth are pledged to the payment of all such rentals.**

**The Bonds are further secured by the guaranty of the Commonwealth, under which the Commonwealth pledges to draw from any funds available in the Treasury of the Commonwealth such sums as may be necessary to cover any deficiency in the amount required for the payment of principal of and interest on the Bonds and to restore the reserve accounts for the Bonds. The good faith and credit of the Commonwealth, as in the case of the Commonwealth's general obligation bonds, are pledged for such payments.**

*In the opinion of Bond Counsel, subject to continuing compliance with certain tax covenants, interest on the Bonds is excluded from gross income for Federal income tax purposes under existing statutes, regulations, rulings and court decisions. However, see "Tax Exemption" herein for a description of the alternative minimum tax on corporations and certain other federal tax consequences of ownership of the Bonds. Bond Counsel is further of the opinion that the Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation.*

The Bonds are offered for delivery when, as and if issued and accepted by the Underwriters, subject to the approval of legality by Brown & Wood, New York, New York, Bond Counsel, and certain other conditions. Certain legal matters will be passed upon for the Underwriters by Rogers & Wells, New York, New York. It is expected that the Bonds will be available for delivery to DTC in New York, New York on or about June 16, 1993.

**The First Boston Corporation**

**Lazard Frères & Co.**

**Lehman Brothers**

**PaineWebber Incorporated**

**Bear, Stearns & Co. Inc.** **Donaldson, Lufkin & Jenrette** Securities Corporation **Goldman, Sachs & Co.**

**Kidder, Peabody & Co.** Incorporated **Merrill Lynch & Co.** **Smith Barney, Harris Upham & Co.** Incorporated

**Dean Witter Reynolds**

*The date of this Official Statement is June 3, 1993.*

† The Indexed Inverse Floaters will be dated the date of delivery thereof.

# $713,480,000
# Puerto Rico Public Buildings Authority

## $128,895,000
## Revenue Refunding Bonds, Series L

### $36,630,000 Series L Fixed Rate Serial Bonds*

| Year (July 1) | Amount | Interest Rate | Price or Yield | Year (July 1) | Amount | Interest Rate | Price or Yield |
|---|---|---|---|---|---|---|---|
| 1997 | $1,460,000 | 4.20% | 4.30% | 2003 | $2,135,000 | 5.30% | 5.40% |
| 1998 | 2,140,000 | 4½ | 4.60 | 2004 | 2,250,000 | 5.40 | 5.50 |
| 1999 | 4,605,000 | 4.70 | 4.80 | 2005 | 2,375,000 | 5.40 | 5.55 |
| 2000 | 2,325,000 | 4.90 | 5.00 | 2006 | 2,500,000 | 5½ | 5.60 |
| 2001 | 2,450,000 | 5.10 | 5.20 | 2009 | 5,735,000 | 5.70 | NRO** |
| 2002 | 2,590,000 | 5.20 | 5.30 | 2010 | 6,065,000 | 5¾ | NRO** |

### $10,520,000 Series L Tax-Exempt Components (TXCs)†, NRO**

| Description of $5,120,000 TXCs Due July 1, 2007* | Description of $5,400,000 TXCs Due July 1, 2008* |
|---|---|
| 5½% Single Coupon TXC | 5.60% Single Coupon TXC |
| 5½% Principal Only TXC | 5.60% Principal Only TXC |
| 5½% Annuity TXC | 5.60% Annuity TXC |
| 5½% Deferred Interest TXC | 5.60% Deferred Interest TXC |
| 5½% Current Interest | 5.60% Current Interest TXC |

### $81,745,000 Series L Term Bonds*

**$44,430,000 5¾% Term Bonds Due July 1, 2016, Yield 5.85%**
**$37,315,000 5½% Term Bonds Due July 1, 2021, Yield NRO****

## $584,585,000
## Public Education and Health Facilities Refunding Bonds, Series M

### $242,520,000 Series M Fixed Rate Serial Bonds*

| Year (July 1) | Amount | Interest Rate | Price or Yield | Year (July 1) | Amount | Interest Rate | Price or Yield |
|---|---|---|---|---|---|---|---|
| 1998 | $ 4,485,000 | 4½% | 4.60% | 2004 | $17,960,000 | 5.40% | 5.50% |
| 1999 | 21,890,000 | 4.70 | 4.80 | 2005 | 22,780,000 | 5.40 | 5.55 |
| 2000 | 18,330,000 | 4.90 | 5.00 | 2006 | 24,030,010 | 5½ | 5.60 |
| 2001 | 19,235,000 | 5.10 | 5.20 | 2009 | 33,430,000 | 5.70 | NRO** |
| 2002 | 20,250,000 | 5.20 | 5.30 | 2010 | 35,355,000 | 5¾ | NRO** |
| 2003 | 24,775,000 | 5.30 | 5.40 | | | | |

### $61,640,000 Series M Tax-Exempt Components (TXCs)†, NRO**

| Description of $30,000,000 TXCs Due July 1, 2007* | Description of $31,640,000 TXCs Due July 1, 2008* |
|---|---|
| 5½% Single Coupon TXC | 5.60% Single Coupon TXC |
| 5½% Principal Only TXC | 5.60% Principal Only TXC |
| 5½% Annuity TXC | 5.60% Annuity TXC |
| 5½% Deferred Interest TXC | 5.60% Deferred Interest TXC |
| 5½% Current Interest TXC | 5.60% Current Interest TXC |

### $46,000,000 Series M Indexed Inverse Floaters Due July 1, 2016, NRO**

| Scheduled Conversion Date | Indexed Inverse Floaters Rate | Minimum Rate | Maximum Rate | Base Rate |
|---|---|---|---|---|
| July 1, 1998 | 11.34% - (1.5 × Index Rate) | 0.00% | 11.34% | 5.70% |

### $254,425,000 Series M Term Bonds*

**$152,290,000 5¾% Term Bonds Due July 1, 2015, Yield 5.85%**
**$ 82,135,000 5½% Term Bonds Due July 1, 2021, Yield 5.85%**

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* Accrued Interest from June 1, 1993 to be added.
** Not Reoffered.
† Each TXC evidences the obligation of the Authority to make payments to the registered owner thereof in the amounts and at the times specified in such TXC. For a description of the TXCs offered by the Authority see "Description of the Bonds — TXCs" and Appendix VI herein.

**The information set forth herein has been obtained from the Authority, the Commonwealth of Puerto Rico, and other official sources that are believed to be reliable, but it is not guaranteed as to accuracy or completeness and is not to be construed as a representation by any Underwriter. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Authority or the Commonwealth of Puerto Rico since the date hereof.**

IN CONNECTION WITH THIS OFFERING THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICES OF THE BONDS OFFERED HEREBY OR OF OUTSTANDING REVENUE OR PUBLIC EDUCATION AND HEALTH FACILITIES BONDS AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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# $713,480,000
# Puerto Rico Public Buildings Authority
**Consisting of**
**$128,895,000 Revenue Refunding Bonds, Series L**
**$584,585,000 Public Education and Health Facilities Refunding Bonds, Series M**
## Guaranteed by the Commonwealth of Puerto Rico

### INTRODUCTION

The purpose of this Official Statement of Puerto Rico Public Buildings Authority (the "Authority"), which includes the cover page and the appendices, is to furnish information with respect to issuance of the Authority's $128,895,000 Puerto Rico Public Buildings Authority Revenue Refunding Bonds, Series L, Guaranteed by the Commonwealth of Puerto Rico (the "1993 Revenue Refunding Bonds") and $584,585,000 Puerto Rico Public Buildings Authority Public Education and Health Facilities Refunding Bonds, Series M, Guaranteed by the Commonwealth of Puerto Rico (the "1993 Public Education and Health Facilities Refunding Bonds"). The 1993 Revenue Refunding Bonds and the 1993 Public Education and Health Facilities Refunding Bonds are hereinafter collectively called the "Bonds". A portion of the Bonds will be delivered as Tax-Exempt Components ("TXCs") and a portion of the 1993 Public Education and Health Facilities Refunding Bonds will be delivered as Indexed Inverse Floaters (the "Indexed Inverse Floaters"). See "Description of the Bonds" herein.

The 1993 Revenue Refunding Bonds will be issued pursuant to Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended (the "Enabling Act"), and under the provisions of Resolution No. 77, adopted November 16, 1970, as supplemented (the "1970 Bond Resolution"). The 1993 Public Education and Health Facilities Refunding Bonds will be issued pursuant to the Enabling Act and under the provisions of Resolution No. 158, adopted February 14, 1978, as supplemented (the "1978 Bond Resolution").

### PLAN OF FINANCING

The 1993 Revenue Refunding Bonds will be issued to refund the following outstanding Puerto Rico Public Buildings Authority Revenue Bonds (the "Refunded Revenue Bonds") on the dates and at the redemption prices (expressed as a percentage of the principal amount to be refunded) set forth below:

| Revenue Bonds | Principal Amount to be Refunded | Maturity Date | Redemption Date | Redemption Price |
|---|---|---|---|---|
| Series B | $ 13,365,000 | July 1, 2002 | July 22, 1993 | 100½% |
| Series H | 53,655,000 | July 1, 1999, 2009, 2017, 2019 | July 1, 1998 | 101½ |
| Series K | 50,460,000 | July 1, 2003-2005, 2007, 2012, 2021 | July 1, 2002 | 101½ |

The 1993 Public Education and Health Facilities Refunding Bonds will be issued to refund the following outstanding Puerto Rico Public Buildings Authority Public Education and Health Facilities Bonds (the "Refunded Public Education and Health Facilities Bonds") on the dates and at the redemption prices (expressed as a percentage of the principal amount to be refunded) set forth below:

| Public Education and Health Facilities Bonds | Principal Amount to be Refunded | Maturity Dates | Redemption Date | Redemption Price |
|---|---|---|---|---|
| Series F | $ 61,885,000 | July 1, 1997-2004, 2012 | July 1, 1996 | 103 % |
| Series G | 79,750,000 | July 1, 1998-2002, 2007, 2016 | July 1, 1997 | 102 |
| Series H | 153,880,000 | July 1, 1998-2002, 2007, 2016 | July 1, 1997 | 102 |
| Series J | 98,310,000 | July 1, 1999, 2009, 2017, 2019 | July 1, 1998 | 101½ |
| Series L | 126,140,000 | July 1, 2003-2005, 2007, 2012, 2021 | July 1, 2002 | 101½ |

The Authority will deposit a portion of the proceeds of the 1993 Revenue Refunding Bonds in escrow with Morgan Guaranty Trust Company of New York, the Fiscal Agent and Bond Registrar under the 1970 Bond Resolution (the "1970 Fiscal Agent") for investment in (i) non-callable direct obligations of the United States and (ii) obligations issued or guaranteed by an agency of the United States or person controlled or supervised by and acting as an instrumentality of the United States pursuant to authority granted by the Congress, the principal of and interest on which when due, with other uninvested moneys, will be sufficient to pay when due the principal of and premium and interest on the Refunded Revenue Bonds. Under the 1970 Bond Resolution, upon such deposit, the Refunded Revenue Bonds will not be deemed to be outstanding for purposes of the 1970 Bond Resolution.

The Authority will deposit a portion of the proceeds of the 1993 Public Education and Health Facilities Refunding Bonds in escrow with The Chase Manhattan Bank (National Association), the Fiscal Agent and Bond Registrar under the 1978 Bond Resolution (the "1978 Fiscal Agent") for investment in (i) non-callable direct obligations of the United States and (ii) obligations issued or guaranteed by an agency of the United States or person controlled or supervised by and acting as an instrumentality of the United States pursuant to authority granted by the Congress, the principal of and interest on which when due, with other uninvested moneys, will be sufficient to pay when due the principal of and premium and interest on the Refunded Public Education and Health Facilities Bonds. Under the 1978 Bond Resolution, upon such deposit, the Refunded Public Education and Health Facilities Bonds will not be deemed to be outstanding for purposes of the 1978 Bond Resolution.

The Refunded Revenue Bonds and the Refunded Public Education and Health Facilities Bonds are hereinafter collectively called the "Refunded Bonds". The refunding will permit the Authority to realize savings in its aggregate debt service requirements for bonded indebtedness.

The adequacy of the amounts so deposited, with the investment earnings thereon, to accomplish the refunding of the Refunded Bonds will be verified by Ernst & Young, the verification agent.

## SOURCES AND USES OF FUNDS

The estimated sources of funds, exclusive of accrued interest, and the estimated uses thereof are set forth below:

| | |
|---|---|
| Sources: | |
| Principal amount of Bonds | $713,480,000 |
| Original Issue Discount | (9,867,757) |
| Total sources | $703,612,243 |
| Uses: | |
| Deposit to escrow fund to defease Refunded Revenue Bonds | $125,092,892 |
| Deposit to escrow fund to defease Refunded Public Education and Health Facilities Bonds | 570,650,560 |
| Deposit to 1978 Reserve Account | 63,802 |
| Underwriting discount and estimated legal, printing and financing expenses | 7,804,989 |
| Total uses | $703,612,243 |

## DESCRIPTION OF THE BONDS

### General

The Bonds will be dated June 1, 1993, except for the Indexed Inverse Floaters as described below which will be dated their date of delivery, and will bear interest at such rates, payable at such times, and will mature on July 1 of the years and in the principal amounts set forth on the inside cover of this Official Statement. The Bonds will be issued in fully registered form, and except as otherwise described below, will be in denominations of $5,000 or any multiple thereof, and when issued will initially be registered only in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), which will act as securities depository for the Bonds (DTC, together with each successor securities depository, the "Securities Depository"). The Bonds are subject to redemption as described below under "Redemption Provisions".

The following information is a summary of the terms and conditions with respect to the Tax Exempt Components and Indexed Inverse Floaters. This summary is not intended to be complete, and the reader is referred to Appendices VI and VII for an explanation of the terms and conditions thereof. Terms used herein that are not otherwise defined shall have the meanings assigned to them in such Appendices.

### TXCs

The $5,120,000 aggregate principal amount of 1993 Revenue Refunding Bonds maturing July 1, 2007 and $5,400,000 aggregate principal amount of 1993 Revenue Refunding Bonds maturing July 1, 2008 (the "TXC 1993 Revenue Refunding Bonds") and the $30,000,000 aggregate principal amount of 1993 Public Education and Health Facilities Refunding Bonds maturing July 1, 2007 and the $31,640,000 aggregate principal amount of 1993 Public Education and Health Facilities Refunding Bonds maturing July 1, 2008 (the "TXC 1993 Public Education and Health Facilities Refunding Bonds"; and with the TXC 1993 Revenue Refunding Bonds the "1993 TXC Bonds") will be delivered as Current Interest Tax Exempt Components ("TXCs").

TXCs will be issued in fully registered form, will be dated June 1, 1993 and will evidence the obligation of the Authority to make one or more interest and/or principal payments to the registered owner of such TXC at the times and in the amounts specified in such TXC. The final payment under any TXC will be made on the date specified in such TXC, which in no event will be later than the applicable maturity date of the related 1993 TXC Bond. The TXCs will be in denominations of $5,000 principal amount or Notional Principal Amount and any multiple thereof. The TXCs are more fully described in Appendix VI, *Description of the Tax Exempt Components.*

**Indexed Inverse Floaters**

The $46,000,000 aggregate principal amount of Public Education and Health Facilities Refunding Bonds maturing July 1, 2016 are being delivered as Indexed Inverse Floaters (the "Indexed Inverse Floaters"). The Indexed Inverse Floaters will be in the principal amount and will mature on the date indicated on the inside cover page of this Official Statement. Interest with respect to the Indexed Inverse Floaters will be payable on each January 1 and July 1, commencing January 1, 1994, and will accrue from the date of initial delivery through the day prior to the Scheduled Conversion Date indicated on the inside cover page of this Official Statement at a rate equal to the Indexed Inverse Floaters Rate (computed as described in Appendix VII under "General") and thereafter at a rate equal to the Base Rate indicated on the inside cover page of this Official Statement until the maturity date thereof. Owners of the Indexed Inverse Floaters may elect, subject to certain conditions, on any Business Day prior to the Scheduled Conversion Date (the "Optional Conversion Date") to convert the interest rate on not less than $5,000,000 principal amount of the Indexed Inverse Floaters to the applicable Converted Rate (see Appendix VII under "Optional Conversion of the Indexed Inverse Floaters"). The Indexed Inverse Floaters will be issued in fully registered form in denominations of $100,000 and any multiple thereof until the Scheduled Conversion Date or the Optional Conversion Date, and thereafter will be in denominations of $5,000 and any multiple thereof. The Indexed Inverse Floaters are more fully described in Appendix VII, *Description of the Indexed Inverse Floaters.*

**Redemption Provisions**

*Optional Redemption.* The 1993 Revenue Refunding Bonds maturing July 1, 2016 may be redeemed at the option of the Authority upon 30 days' notice from any moneys available therefor, in whole on July 1, 2003 or on any date thereafter, or in part, as directed by the Authority, on July 1, 2003 or on any date thereafter, at the following prices (expressed as a percentage of the principal amount), plus accrued interest to the date fixed for redemption:

| Period During Which Redeemed (Both Dates Included) | Redemption Price |
|---|---|
| July 1, 2003 through June 30, 2004 | 101½% |
| July 1, 2004 through June 30, 2005 | 100¾ |
| July 1, 2005 and thereafter | 100 |

The 1993 Public Education and Health Facilities Refunding Bonds maturing July 1, 2015, 2016 and 2021 may be redeemed at the option of the Authority upon 30 days' notice from any moneys available therefor, in whole on July 1, 2003 or on any date thereafter, or in part, as directed by the Authority, on July 1, 2003 or on any date thereafter, at the following prices (expressed as a percentage of the principal amount), plus accrued interest to the date fixed for redemption:

| Period During Which Redeemed (Both Dates Included) | Redemption Price |
|---|---|
| July 1, 2003 through June 30, 2004 | 101½% |
| July 1, 2004 through June 30, 2005 | 100¾ |
| July 1, 2005 and thereafter | 100 |

*Mandatory Redemption.* The 1993 Revenue Refunding Bonds maturing July 1, 2016 and July 1, 2021 shall be redeemed upon 30 days' notice in part on July 1, 2011 and July 1, 2017, respectively, and on each July 1 thereafter for which there are Amortization Requirements as set forth below in the principal amount equal to the respective Amortization Requirements for such 1993 Revenue Refunding Bonds (less the principal amount of any such 1993 Revenue Refunding Bonds retired by purchase) from moneys in the Sinking Fund established by the 1970 Bond Resolution, at par plus accrued interest to the date fixed for redemption as follows:

| | Amortization Requirements for 1993 Revenue Refunding Bonds due July 1 | |
|---|---|---|
| July 1 | 2016 | 2021 |
| 2011 | $ 6,410,000 | |
| 2012 | 6,775,000 | |
| 2013 | 7,170,000 | |
| 2014 | 7,580,000 | |
| 2015 | 8,015,000 | |
| 2016 | 8,480,000† | |
| 2017 | | $ 8,965,000 |
| 2018 | | 9,460,000 |
| 2019 | | 9,985,000 |
| 2020 | | 4,335,000 |
| 2021 | | 4,570,000† |
| | $44,430,000 | $37,315,000 |
| Average life (years) | 20.72 | 25.68 |

† Final Maturity.

The 1993 Public Education and Health Facilities Refunding Bonds maturing July 1, 2015, July 1, 2016 and July 1, 2021 shall be redeemed upon 30 days' notice in part on July 1, 2011, July 1, 2015 and July 1, 2017, respectively, and on each July 1 thereafter for which there are Amortization Requirements as set forth below in the principal amount equal to the respective Amortization Requirements for such 1993 Public Education and Health Facilities Refunding Bonds (less the principal amount of any such 1993 Public Education and Health Facilities Refunding Bonds retired by purchase) from moneys in the Sinking Fund established by the 1978 Bond Resolution, at par plus accrued interest to the date fixed for redemption as follows:

| | Amortization Requirements for 1993 Public Education and Health Facilities Refunding Bonds due July 1 | | |
|---|---|---|---|
| July 1 | 2015 | 2016 | 2021 |
| 2011 | $ 37,410,000 | | |
| 2012 | 39,600,000 | | |
| 2013 | 27,825,000 | | |
| 2014 | 29,425,000 | | |
| 2015 | 18,030,000† | $13,095,000 | |
| 2016 | | 32,905,000† | |
| 2017 | | | $18,895,000 |
| 2018 | | | 19,935,000 |
| 2019 | | | 21,035,000 |
| 2020 | | | 10,835,000 |
| 2021 | | | 11,435,000† |
| | $152,290,000 | $46,000,000 | $82,135,000 |
| Average life (years) | 19.73 | 22.77 | 25.76 |

† Final Maturity

*Notice of Redemption.* At least thirty (30) days prior to any redemption, notice thereof will be sent by certified mail or other agreed method to DTC or if the book-entry only system is discontinued as described under the caption "Book-Entry Only System", by first class mail, postage prepaid, to the registered owners of the Bonds to be redeemed. If less than all of the Bonds of any one maturity are called for redemption, the particular Bonds or portions thereof to be redeemed will be selected by the appropriate Fiscal Agent by lot by such method as it may determine, except that so long as the book-entry only system shall remain in effect, the selection of the Bonds to be redeemed shall be determined as provided under the caption "Book-Entry Only System." Each notice of redemption shall contain, among other things, the CUSIP identification number of the Bonds (or portions thereof) being called for redemption, the redemption date and price and the address at which such Bonds are to be surrendered for payment of the redemption price. Any defect in such notice or the failure so to mail any such notice to DTC in respect of, or the registered owner of, any Bond will not affect the validity of the proceedings for the redemption of any other Bond.

**Book-Entry Only System**

The following information concerning DTC and DTC's book-entry system has been obtained from DTC and neither the Authority nor the Underwriters take any responsibility for the accuracy thereof.

DTC is to act as securities depository for the Bonds. The Bonds are to be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee). One fully-registered Bond certificate of each maturity and designation will be issued for each maturity of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC. If, however, the aggregate principal amount of any maturity exceeds $150 million, one certificate will be issued with respect to each $150 million of principal amount and an additional certificate will be issued with respect to any remaining principal amount of such maturity.

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Act of 1934. DTC holds securities that its participants ("Participants") deposit with DTC. DTC also facilitates the settlement among Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in Participants' accounts, thereby eliminating the need for physical movement of securities certificates. Direct Participants include securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is owned by a number of its Direct Participants and by the New York Stock Exchange, Inc., the American Stock Exchange, Inc., and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as securities brokers and dealers, banks, and trust companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). The Rules applicable to DTC and its Participants are on file with the Securities and Exchange Commission.

Purchases of the Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC's records. The ownership interest of each actual purchaser of each Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co. The deposit of Bonds with DTC and their registration in the name of Cede & Co. effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC's records affect only the identity of the Direct Participants to whose accounts such

Bonds are credited, which may or may not be the Beneficial Owners. The Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to Cede & Co. If less than all of the Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. will consent or vote with respect to the Bonds. Under its usual procedures, DTC mails an Omnibus Proxy to the issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Bonds are to be made to DTC. DTC's practice is to credit Direct Participants' accounts on payable date in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on payable date. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer from or registered in "street name," and will be the responsibility of such Participant and not of DTC, the 1970 Fiscal Agent, the 1978 Fiscal Agent, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to DTC is the responsibility of the Authority, the 1970 Fiscal Agent or the 1978 Fiscal Agent or disbursement of such payments to Direct Participants shall be the responsibility of DTC, and disbursement of such payments to the Beneficial owners shall be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Bonds at any time by giving reasonable notice to the Authority, the 1970 Fiscal Agent or the 1978 Fiscal Agent. Under such circumstances, in the event that a successor securities depository is not obtained, Bond certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered.

*The Authority, the 1970 Fiscal Agent and the 1978 Fiscal Agent will have no responsibility or obligation to such DTC Participants, Indirect Participants, or the persons for whom they act as nominees with respect to the payments to or the providing of notice for the DTC Participants, the Indirect Participants, or the Beneficial Owners. Payments made to DTC or its nominee shall satisfy the obligations of the Authority to the extent of such payments.*

In the event that such book-entry only system is discontinued for the 1993 Revenue Refunding Bonds, the following provisions will apply to the 1993 Revenue Refunding Bonds: principal of the 1993 Revenue Refunding Bonds and redemption premium, if any, thereon will be payable in lawful money of the United States of America at the corporate trust office of the 1970 Fiscal Agent in New York, New York. Interest on the 1993 Revenue Refunding Bonds will be payable on each January 1 and July 1, by check mailed to the respective addresses of the registered owners thereof as shown on the registration books of the Authority maintained by the 1970 Fiscal Agent as of the close of business on the record date therefor as set forth in the 1970 Bond Resolution. The 1993 Revenue Refunding Bonds will be issued only as fully registered bonds in denominations of $5,000 or any multiple thereof, except in the case of the TXCs which will be issued in denominations of $5,000 principal amount or Notional Principal Amount, or any multiple thereof. The transfer of 1993 Revenue Refunding Bonds will be registrable and 1993 Revenue Refunding Bonds may be exchanged at the corporate trust office of the 1970 Fiscal Agent in New York, New York upon the payment of any taxes or other governmental charges required to be paid with respect to such transfer or exchange.

In the event that such book-entry only system is discontinued for the 1993 Public Education and Health Facilities Refunding Bonds, the following provisions will apply to the 1993 Public Education and Health Facilities Refunding Bonds: principal of the 1993 Public Education and Health Facilities Refunding Bonds and redemption premium, if any, thereon will be payable in lawful money of the United States of America at the principal corporate trust office of the 1978 Fiscal Agent in New York, New York. Interest on the 1993 Public Education and Health Facilities Refunding Bonds will be payable on each January 1 and July 1, by check mailed to the respective addresses of the registered owners thereof as shown on the registration books of the Authority maintained by the 1978 Fiscal Agent as of the close of business on the record date therefor as set forth in the 1978 Bond Resolution. The 1993 Public Education and Health Facilities Refunding Bonds will be issued only as fully registered bonds in denominations of $5,000 or any multiple thereof, except in the case of the Indexed Inverse Floaters which will be issued in denominations of $100,000 and any multiple thereof until the Scheduled Conversion Date or Optional Conversion Date, and the TXCs which will be issued in denominations of $5,000 principal amount or Notional Principal Amount, or any multiple thereof. The transfer of 1993 Public Education and Health Facilities Refunding Bonds will be registrable and 1993 Public Education and Health Facilities Refunding Bonds may be exchanged at the principal corporate trust office of the 1978 Fiscal Agent in New York, New York upon the payment of any taxes or other governmental charges required to be paid with respect to such transfer or exchange.

For every transfer of the Bonds, the Beneficial Owner may be charged a sum sufficient to cover any tax or other governmental charge that may be imposed in relation thereto.

## SECURITY

### Security for the Revenue Bonds

The 1993 Revenue Refunding Bonds together with the $133,594,258 Revenue Bonds (calculated by excluding the Refunded Revenue Bonds and all accretion on outstanding capital appreciation Revenue Bonds) outstanding as of the date hereof and any additional Revenue Bonds hereafter issued under the 1970 Bond Resolution (collectively the "Revenue Bonds") will be secured equally and ratably by a pledge of rentals of the office buildings financed by Revenue Bonds and leased by the Authority to various departments, agencies and instrumentalities of the Commonwealth of Puerto Rico (the "Commonwealth"). The Enabling Act provides that the good faith and credit of the Commonwealth are pledged for the payment of rentals under any lease agreement with any department of the Commonwealth and to the making of advances by the Secretary of the Treasury of the Commonwealth to the Authority of any unpaid portion of rentals payable to the Authority by any agency or instrumentality of the Commonwealth. In addition, the Commonwealth guarantees payment of the principal of and interest on the Revenue Bonds and restoration of the reserve account established by the 1970 Bond Resolution (the "1970 Reserve Account").

The rentals received in respect of the office buildings financed by Revenue Bonds and leased by the Authority to various departments, agencies and instrumentalities of the Commonwealth are not available to be applied to the payment of any of the Public Education and Health Facilities Bonds.

### Security for the Public Education and Health Facilities Bonds

The 1993 Public Education and Health Facilities Refunding Bonds together with the $344,924,711 Public Education and Health Facilities Bonds (calculated by excluding the Refunded Public Education and Health Facilities Bonds and all accretion on outstanding capital appreciation Public Education and Health Facilities Bonds) outstanding as of the date hereof and any additional Public Education and Health Facilities Bonds hereafter issued under the 1978 Bond Resolution (collectively, the "Public Education and Health Facilities Bonds") will be secured equally and ratably by a pledge of the rentals of facilities financed by Public Education and Health Facilities Bonds and leased by the Authority to the Department of Education of the Commonwealth (the "Department of Education") and the Department of Health of the Commonwealth (the "Department of Health"). Under the Enabling Act, the good faith and credit of the Commonwealth are pledged for the payment of rentals under any lease agreement between the Authority and any department of the Commonwealth. In addition, the Commonwealth guarantees payment of the principal of and interest on the Public Education and Health Facilities Bonds and restoration of the reserve account established by the 1978 Bond Resolution (the "1978 Reserve Account").

The rentals received in respect of public education and health facilities financed by Public Education and Health Facilities Bonds and leased by the Authority to the Department of Education and the Department of Health are not available to be applied to the payment of any of the Revenue Bonds.

### Commonwealth Guaranty of the Bonds

As provided in Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (the "Guaranty Act"), the Commonwealth guarantees, among other things, the payment of the principal of and interest on the Bonds and the restoration of the 1970 Reserve Account and the 1978 Reserve Account to the extent described herein. The provisions of the Guaranty Act relating to such guaranty are as follows:

> "The Commonwealth of Puerto Rico hereby guarantees payment of the principal and the interest on bonds outstanding at any one time, in an aggregate principal amount not exceeding $1,200,000,000 issued from time to time by the Public Buildings Authority for any of its purposes authorized by law. The bonds covered by this guaranty shall be those specified by the Authority, and a statement of such guaranty shall be set forth on the face of such bonds. If at any time the revenues or income, and any other moneys of the Authority, pledged for the payment of the principal and the interest on such bonds, are not sufficient to pay such principal and interest as the same fall due, or to maintain the reserve fund that the Authority has pledged itself to maintain for

such bonds, the Secretary of the Treasury shall draw from any funds available in the Treasury of Puerto Rico, such sums as may be necessary to cover the deficiency in the amount required for the payment of such principal and interest and to restore said reserve fund to the maximum requirement agreed to by the Authority, and shall direct that the sums so drawn be applied to such payment and purpose. For the purposes of this Section, bonds shall not be deemed to be outstanding, which are not deemed to be outstanding under the provisions of the Resolution or Resolutions, pursuant to which such bonds were issued. The good faith and credit of the Commonwealth of Puerto Rico are hereby pledged for such payments."

The Bonds have been specified by the Authority to be guaranteed by the Commonwealth under the Guaranty Act. The Authority has previously issued $1,931,958,970 of bonds which are guaranteed under the Guaranty Act, of which $1,145,248,970 of such bonds are outstanding (calculated by excluding the accretion on capital appreciation Bonds) on the date hereof. $1,191,988,000 of guaranteed bonds will be outstanding following issuance of the Bonds. The Authority has submitted legislation to the Legislature of Puerto Rico to increase the aggregate principal amount of bonds that may be guaranteed by the Commonwealth by $300,000,000 to $1,500,000,000.

Upon the deposit of moneys and United States government obligations as set forth under *Plan of Financing,* the Refunded Bonds will not be deemed to be outstanding under the 1970 Bond Resolution and the 1978 Bond Resolution, as applicable, and will no longer be entitled to the guaranty of the Commonwealth under the Guaranty Act.

To date, no payments have ever been required under the Guaranty Act.

**Opinion of the Attorney General of the Commonwealth**

Prior to delivery of the Bonds the Attorney General of the Commonwealth will have rendered his opinion to the Authority stating:

"I have examined Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended, creating the Public Buildings Authority (the "Authority") as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico exercising public and essential governmental functions. I have also examined Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (the "Guaranty Act"), providing for the guaranty of the Commonwealth of Puerto Rico of the payment of the principal of and interest on a principal amount of bonds of the Authority outstanding at any one time, not exceeding $1,200,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose. I have also examined the Puerto Rico Constitution and such other laws of the Commonwealth of Puerto Rico as I consider necessary for the purpose of the following opinion.

From such examination I am of the opinion that:

1. The Authority is lawfully authorized to specify up to $1,200,000,000, aggregate principal amount of bonds of the Authority outstanding at any one time, issued for any of its authorized purposes, to be covered by the guaranty of the Commonwealth of Puerto Rico under the Guaranty Act, and the Commonwealth of Puerto Rico will be obligated to pay the principal of and the interest on the bonds so specified to be covered by said guaranty and to restore the reserve funds for such bonds to the maximum requirements agreed to by the Authority, if and to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient to make such payments as the same become due or to maintain the reserve funds for such bonds that the Authority has pledged itself to maintain.

2. Any amounts required to be paid by the Commonwealth of Puerto Rico under said guaranty will constitute 'public debt' within the meaning of Section 8 of Article VI of the Puerto Rico Constitution which provides:

> 'In case the available revenues including surplus for any fiscal year are insufficient to meet the appropriations made for that year, interest on the public debt and amortization thereof shall first be paid, and other disbursements shall thereafter be made in accordance with the order of priorities established by law.'

and will accordingly be entitled to the same priority of payment under the Section as the direct bonded indebtedness of the Commonwealth.

3. Because of its sovereign immunity the Commonwealth cannot be sued without the consent of the Legislature of Puerto Rico. However, the Secretary of the Treasury can be required in a court of justice under the provisions of Section 2 of Article VI of the Puerto Rico Constitution to apply the available revenues including surplus to the payment of interest on the public debt and the amortization thereof in any case provided for by Section 8 of Article VI, including any payments required to be made under said guaranty, at the suit of any holder of bonds issued by the Authority and guaranteed pursuant to the Guaranty Act.

4. The Commonwealth guaranty of the $128,895,000 Public Buildings Authority Revenue Refunding Bonds, Series L, Guaranteed by the Commonwealth of Puerto Rico and, $584,585,000 Public Buildings Authority Public Education and Health Facilities Refunding Bonds, Series M, Guaranteed by the Commonwealth of Puerto Rico, and the Authority's obligation to maintain the reserve account in respect of said bonds at the required levels constitutes a general obligation of the Commonwealth to which its full faith and credit and taxing power are pledged.

5. Although without specific judicial decision on point, I firmly understand and am of the opinion that, for purposes of the principal amount limitation expressed in the Guaranty Act, the initial principal amount of any capital appreciation bonds constitutes the principal amount of such bonds until such bonds are retired and any accreted value above said initial principal amount constitutes interest on such bonds."

**Lease Agreements**

In accordance with the provisions of the 1970 Bond Resolution, the Authority has entered into lease agreements with various departments, agencies, instrumentalities or municipalities of the Commonwealth in respect of office buildings financed by the issuance of Revenue Bonds. The lease agreements require the lessees to pay to the Authority in substantially equal monthly installments such annual rentals as in the aggregate will be sufficient to pay, as the same come due, the interest on, principal of (including any Amortization Requirements) and redemption premium, if any, on the Revenue Bonds and the cost of maintaining, repairing and operating such facilities. Each lease agreement with respect to a facility or facilities terminates when the Revenue Bonds which were issued to finance the acquisition or construction of such facility or facilities have been paid in full. All lease agreements provide for the adjustment of rentals so that the total amounts payable will be sufficient to meet the required debt service charges and operations and maintenance expenses, including the replacement of equipment. In connection with the issuance of the Bonds and certain other refunding bonds previously issued by the Authority, the Authority will amend the lease agreements to reduce the rental payments due thereunder so as to reflect the reduction in debt service as a result of such issuances. Each lease agreement provides that the obligation of the lessee to pay rentals is absolute and unconditional.

In accordance with the provisions of the 1978 Bond Resolution, the Authority has entered into lease agreements with the Department of Education with respect to the public education facilities financed by the issuance of Public Education and Health Facilities Bonds and with the Department of Health with respect to the health facilities financed by the issuance of Public Education and Health Facilities Bonds. The lease agreements require the lessees to pay to the Authority annual rentals in substantially equal monthly installments. The rentals are calculated to take into account the following factors, (1) the interest on, principal of, (including any Amortization Requirements) and redemption premium, if any, on Public Education and Health Facilities Bonds issued to finance such facilities, (2) any amounts necessary to provide and maintain the 1978 Reserve Account, (3) any amounts necessary to pay the general administrative expenses of the

Authority in connection with such facilities, and (4) any amounts necessary to provide and maintain a reserve fund for the replacement of major items of equipment comprising a portion of such facilities. The lease agreements also require the lessees to pay certain amounts on account of the principal of and interest on outstanding notes issued to finance the leased facilities. Each lease agreement with respect to a facility or facilities terminates when all Public Education and Health Facilities Bonds issued, and all other obligations incurred by the Authority under the 1978 Bond Resolution in connection with such facility or facilities, are paid in full. All lease agreements provide for the adjustment of rentals so that the total amounts payable will be sufficient to meet the required debt service charges. In connection with the issuance of the Bonds and certain other refunding bonds previously issued by the Authority, the Authority will amend the lease agreements to reduce the rental payments due thereunder so as to reflect the reduction in debt service as a result of such issuances. Each lease agreement provides that the obligation of the lessee to pay rentals is absolute and unconditional.

Monthly rental payments for office buildings are not due until the last day of the month and are generally not received by the Authority until after the close of the month. Monthly rental payments for public education and health facilities are due on or before the 10th day of each month. Although there have been delays in the payment of monthly rentals, there has been no default or delay in the payment of the principal of or interest on any indebtedness of the Authority and no recourse to the 1970 Reserve Account established under the 1970 Bond Resolution or the 1978 Reserve Account established under the 1978 Bond Resolution.

Included among the operating and maintenance expenses that are required to be paid under the lease agreements by the lessee is the cost of insurance premiums. In December 1992, the property and casualty insurance company that insured all Commonwealth-owned property (including approximately $1.3 billion of the Authority's properties) against losses from fire, hurricanes or other natural disasters and personal liability was placed in court-ordered liquidation. The Commonwealth and the Authority are endeavoring to seek alternate insurance arrangements, both directly and through insurance brokers, but to date they have not yet been able to secure such alternate insurance arrangements at commercially reasonable rates. The Authority's lease agreements provide that the lessee's obligation to make rental payments is absolute and unconditional, regardless of whether the facilities leased are damaged, destroyed or otherwise become unusable for any period of time and regardless of any default by the Authority thereunder. The lease agreements further provide that the Authority is obligated at the expense of the lessee to obtain insurance to cover required rental payments during periods when facilities become unusable as a result of damage or destruction, to the extent such insurance is commercially obtainable. To date, the Authority has been unable to make alternate rental insurance arrangements as well. See *"Insurance Matters"* in Appendix I.

For further information regarding certain provisions required by the 1970 Bond Resolution and the 1978 Bond Resolution to be included in each lease agreement in respect of facilities financed by the Bonds, see, respectively, *Summary of Certain Provisions of the 1970 Bond Resolution* and *Summary of Certain Provisions of the 1978 Bond Resolution.*

**Pledge of the Commonwealth to Pay or Advance Rentals**

Under the 1970 Bond Resolution and the 1978 Bond Resolution, the Authority has covenanted that if any department, agency, instrumentality or municipality fails to pay any rent when due, the Authority will promptly notify the Secretary of the Treasury of the Commonwealth.

As provided in the Enabling Act, the good faith and credit of the Commonwealth are pledged for the payment of the rent under any lease contract with the Authority executed by any of the Commonwealth's executive departments (including, among others, the Department of Education and the Department of Health) and any other governmental body created by the Legislature and depending mainly on legislative appropriations to meet its operating expenses.

The Enabling Act also provides that if any rent payable to the Authority by any agency or instrumentality (other than a department) under a lease contract is not paid when due, then the Commonwealth shall advance the unpaid balance to the Authority. The Commonwealth pledges its good faith and credit to the making of such advances. Any advances so made are required to be reimbursed by the particular agency or instrumentality involved.

Payments or advances of rentals by the Commonwealth, as described above, are subject to annual appropriations by the Legislature, which appropriations are legally required to be made. However, the obligation to make such appropriations is not legally enforceable in view of the sovereign immunity of the Commonwealth, and, unlike the obligation to make payments under the guaranty of the Bonds, the obligation to pay or advance rentals does not constitute "public debt" within the meaning of Section 8 of Article VI of the Puerto Rico Constitution.

**Reserve Accounts**

Under the 1970 Bond Resolution, the Authority is obligated, upon the delivery of any Revenue Bonds, to deposit in the 1970 Reserve Account from bond proceeds or other available funds the amount necessary so that the balance in the 1970 Reserve Account will equal 50% of the maximum aggregate annual debt service on all outstanding Revenue Bonds. Under the 1970 Bond Resolution, the Authority is permitted to deposit to the credit of the 1970 Reserve Account a Reserve Account Insurance Policy or a Reserve Account Letter of Credit to meet all or a portion of the required balance in the 1970 Reserve Account. As of December 31, 1992, moneys, securities and a Reserve Account Letter of Credit equal to $13,995,613 in the aggregate were held in the 1970 Reserve Account by the 1970 Fiscal Agent, which amount is in excess of the amount required to be on deposit in the 1970 Reserve Account. As of December 31, 1992, the amount available to be drawn under the Reserve Account Letter of Credit deposited to the credit of the 1970 Reserve Account was $13,614,467. The Commonwealth's guaranty under the Guaranty Act includes the restoration to the Authority for any sums withdrawn from the 1970 Reserve Account to pay principal of and interest on the Revenue Bonds to the maximum requirement agreed to by the Authority.

Under the 1978 Bond Resolution, the Authority is obligated to maintain in the 1978 Reserve Account at any time an amount equal to the greater of (1) 100% of the maximum aggregate annual interest on all Public Education and Health Facilities Bonds then outstanding and (2) 50% of the maximum aggregate annual debt service on all Public Education and Health Facilities Bonds then outstanding. At present, the amount required to be on deposit on the 1978 Reserve Account is based on (1) above. Under the 1978 Bond Resolution, the Authority is permitted to deposit to the credit of the 1978 Reserve Account a Reserve Account Insurance Policy or a Reserve Account Letter of Credit to meet all or a portion of the required balance in the 1978 Reserve Account. As of December 31, 1992, a Reserve Account Letter of Credit equal to $58,760,583 was held in the 1978 Reserve Account by the 1978 Fiscal Agent, which amount is equal to the amount required to be on deposit in the 1978 Reserve Account. As of December 31, 1992, the amount available to be drawn under the Reserve Account Letter of Credit deposited to the credit of the 1978 Reserve Account was $58,760,583. The Commonwealth's guaranty under the Guaranty Act includes the restoration to the Authority for any sums withdrawn from the 1978 Reserve Account to pay principal of and interest on the Public Education and Health Facilities Bonds to the maximum requirement agreed to by the Authority.

The Reserve Account Letters of Credit currently deposited in each Reserve Account were issued by The Industrial Bank of Japan, Limited, New York Branch ("IBJ") (each, an "IBJ Reserve Account Letter of Credit" and, collectively, the "IBJ Reserve Account Letters of Credit") in the stated amounts set forth above. The Authority, upon prior notice, may cause the IBJ Reserve Account Letters of Credit to be terminated if it chooses to substitute them with cash or an alternate Reserve Account Letter of Credit or a Reserve Account Insurance Policy as permitted by the applicable Bond Resolution. The scheduled expiration date of the IBJ Reserve Account Letters of Credit is July 1, 2000. Upon the issuance of the Bonds, the stated amount of the IBJ Reserve Account Letter of Credit on deposit in the 1970 Reserve Account, together with any moneys or securities therein on deposit, will equal at least $13,614,172 (representing an amount equal to 50% of the maximum aggregate annual debt service on the Revenue Bonds) and the stated amount of the IBJ Reserve Account Letter of Credit on deposit in the 1978 Reserve Account, together with any moneys or securities therein on deposit, will equal at least $58,824,384 (representing an amount equal to the greater of maximum annual interest on the outstanding Public Education and Health Facilities Bonds and 50% of the maximum aggregate debt service on the Public Education and Health Facilities Bonds).

The IBJ Reserve Account Letters of Credit authorize the 1970 Fiscal Agent and the 1978 Fiscal Agent to make drawings under the respective Reserve Account Letters of Credit for the payment of any amount required to be paid out of moneys in the Reserve Account to which such Reserve Account Letter of Credit relates after the withdrawal from the applicable Reserve Account of all cash and securities therein. In addition, the applicable Fiscal Agent must draw on such Reserve Account Letter of Credit on the interest payment date before its expiration to satisfy the funding requirements of the Reserve Account to which such Reserve Account Letter of Credit relates resulting solely from the expiration of such Reserve Account Letter of Credit.

Upon any drawing, the stated amount of the respective IBJ Reserve Account Letters of Credit will be reduced by the amount of such drawing. Subject to any permanent reduction in the stated amount pursuant to the respective IBJ Reserve Account Letters of Credit, the amount of any drawing (except the drawing relating to the expiration of such Letters of Credit as described above) will be automatically reinstated effective on the date IBJ is reimbursed in full for such drawing. If at any time during which the IBJ Reserve Account Letters of Credit are outstanding there exists any other Reserve Account Letter of Credit or Reserve Account Insurance Policy deposited in the 1970 Reserve Account or the 1978 Reserve Account, as the case may be, the relevant Fiscal Agent is required to make drawings among the relevant IBJ Reserve Account Letter of Credit and such other facilities on a pro rata basis.

Upon the occurrence of an event of default under the applicable reimbursement agreements between IBJ and the Authority, including but not limited to (a) failure by the Authority to pay any amounts (including fees) due thereunder and (b) failure by the Commonwealth to appropriate moneys for lease rentals or under the Guaranty Act, IBJ may (i) demand all reimbursement obligations owing by the Authority to be immediately due and payable by the Authority without further notice or action, or (ii) upon the occurrence of an event of default specified in clause (a) above, refuse to reinstate the applicable IBJ Reserve Account Letter of Credit upon reimbursement for any pre-termination drawing, or (iii) require the Authority (x) to cause to be deposited into the applicable Reserve Account cash, securities or one or more Reserve Account Letters of Credit or Reserve Account Insurance Policies in an amount equal to the full amount required to be on deposit in such Reserve Account pursuant to the applicable Bond Resolution (without giving effect to the existence of the IBJ Reserve Account Letter of Credit related thereto), and solely upon fulfillment of the requirement specified in clause (x) above, (y) to cause the applicable Fiscal Agent to deliver the applicable IBJ Reserve Account Letter of Credit to IBJ for cancellation, or (iv) proceed to enforce all remedies available to it under the applicable reimbursement agreement or Bond Resolution and applicable law or (v) take any one or more of the actions specified in clauses (i) through (iv) above as IBJ so elects.

For additional information concerning the provisions of the 1970 Reserve Account and the 1978 Reserve Account, see, respectively, "1970 Sinking Fund" under *Summary of Certain Provisions of the 1970 Bond Resolution* and "1978 Sinking Fund" under *Summary of Certain Provisions of the 1978 Bond Resolution.*

## PROVISIONS RELATING TO PUBLIC DEBT OF THE COMMONWEALTH

### Payment of Public Debt

The Constitution of Puerto Rico provides that public debt of the Commonwealth will constitute a first claim on available Commonwealth revenues. Public debt of the Commonwealth includes general obligation bonds and notes of the Commonwealth and, according to opinions heretofore rendered by the Attorney General of the Commonwealth, also any payments required to be made by the Commonwealth under its guarantees of bonds and notes issued by its public instrumentalities. Any such guaranty payments, including guaranty payments under the Guaranty Act, are equal in their claim on such available Commonwealth revenues to claims for the payment of debt service on general obligation bonds and notes of the Commonwealth. Under Act No. 269 of the Legislature of Puerto Rico, approved May 11, 1949, as amended, the Commonwealth funds from property taxes a special fund for the Amortization and Redemption of General Obligations Evidenced by Bonds and Promissory Notes, for application to the payment of general obligation bonds and notes of the Commonwealth.

The Commonwealth has allocated certain motor vehicle fuel taxes and license fees to the Puerto Rico Highway and Transportation Authority. However, the taxes so allocated are subject to first being applied to payment of the principal of and interest on the Commonwealth public debt, but only if and to the extent that all other available revenues of the Commonwealth are insufficient for that purpose. The Commonwealth has never applied such taxes to the payment of its public debt.

While the Commonwealth has sovereign immunity from suit, judgment and execution in respect of its public debt, the Constitution specifically empowers a holder of bonds and notes evidencing public debt to bring suit against the Secretary of the Treasury to require application of available revenues, including surplus, to the payment of principal of and interest on public debt when due.

The Commonwealth has never defaulted on the payment of principal of or interest on any of its public debt.

### Debt Limitation

Section 2 of Article VI of the Constitution of Puerto Rico provides that direct obligations of the Commonwealth evidenced by full faith and credit bonds or notes shall not be issued if the maximum debt service payable in any fiscal year on such bonds or notes to be issued and on such bonds or notes theretofore issued and outstanding, when added to any debt service paid in the preceding fiscal year by the Commonwealth on bonds or notes guaranteed by the Commonwealth, shall exceed 15% of the adjusted average annual internal revenues of the Commonwealth for the two preceding fiscal years.

This limitation does not constrain the amount of debt that the Commonwealth may guarantee unless the sum of the debt service that has been paid in the preceding fiscal year from funds in the Commonwealth Treasury on guaranteed bonds and notes and the maximum debt service payable in any fiscal year on outstanding general obligation bonds and notes exceeds 15% of adjusted average annual internal revenues of the Commonwealth for the two preceding fiscal years. So long as the 15% limitation is exceeded, the Commonwealth may not make further guarantees of bonds or notes.

Certain revenues, such as Federal excise taxes on offshore shipments and customs, which are collected by the United States Government and returned to the Commonwealth Treasury, and motor vehicle fuel taxes which are allocated to the Highway and Transportation Authority, are not included as revenues for the purpose of calculating the debt limit, although they may be available, once received, for the payment of debt service.

Maximum annual debt service for the Commonwealth's outstanding general obligation debt is $367,892,000. See "Debt Service Requirements for Commonwealth Direct and Guaranteed Debt" under *Debt* in Appendix I. That amount is estimated to equal 9.891% of the adjusted average annual internal revenues of $3,719,282,697 for the two fiscal years ended June 30, 1991 and 1992.

## THE AUTHORITY

### General

The Authority, a body corporate and politic constituting an instrumentality of the Commonwealth exercising public and essential governmental functions, was created on June 19, 1958 by the Enabling Act.

Under the Enabling Act, the primary duties of the Authority are to design and construct office buildings, quarters, courts, warehouses, shops, schools, health facilities, social welfare facilities and related facilities for lease to the Commonwealth or any of its departments, agencies, instrumentalities or municipalities.

The Authority has broad powers under the Enabling Act, including among others: to make contracts and to execute all instruments necessary or convenient for the exercise of any of its powers; to acquire any kind of properties and rights therein in any lawful manner, including, without limitation, acquisition by purchase, either by agreement or through the exercise of the power of eminent domain, lease or bequest, and to possess, lease, use and operate any properties or facilities, to prepare plans, projects and cost estimates for the construction, improvement or repair of any property or facility; to contract with any Commonwealth department, agency or official, or with any private person or entity with regard to the administration of any properties or facilities of the Authority; to borrow money and issue bonds of the Authority for any of its corporate purposes, and to secure payment of its bonds by pledge of all or any of its properties, revenues and income; and to do all acts necessary or convenient to carry out the powers granted to it.

### Management

The Authority is governed by seven members, all of whom are appointed for five-year terms by the Governor of Puerto Rico with the advice and consent of the Senate. There is currently one vacancy on the Board.

The present members of the Board of the Authority are:

| | | Expiration of Term of Office |
|---|---|---|
| Luis E. Dubón, III, Esq., Chairman | Lawyer | June 30, 1993 |
| Pedro J. Díaz - Molina | Insurance Agent | June 30, 1993 |
| Alberto Carrero | Engineer | June 30, 1993 |
| Rigoberto Figueroa - Figueroa | Businessman | July 19, 1995 |
| Aníbal L. Arsuaga | Businessman | June 30, 1993 |
| José L. Castillo | Businessman | June 30, 1993 |

The current Executive Director of the Authority is Raimundo Matos-Iglesias. Mr. Matos-Iglesias is a civil engineer and a graduate of the University of Puerto Rico's Mayagüez Campus. In the past he has held various governmental positions including Executive Director of Puerto Rico Urban Renewal and Housing Corporation. At the time of his appointment he was self employed as an engineer.

### Debt

The following table sets forth the outstanding debt of the Authority.

| | As of February 28, 1993(1) | As Adjusted(2) |
|---|---|---|
| Bonded Debt: | | |
| Bonds issued under the 1970 Bond Resolution | $ 260,459,258 | $ 262,489,258 |
| Bonds issued under the 1978 Bond Resolution | 884,789,712 | 929,509,711 |
| Total bonded debt | 1,145,248,970 | 1,191,998,969 |
| Office building notes | -0- | -0- |
| Public education and health facilities notes | -0- | -0- |
| Other(3) | 2,133,030 | 2,133,030 |
| Total debt | $1,147,382,000 | $1,194,131,999 |

(1) Calculated by excluding all interest accretion on outstanding capital appreciation Bonds from their respective dates of issuance.

(2) Reflects the outstanding debt of the Authority as of the date of issuance of the Bonds and the refunding of the Refunded Bonds.

(3) Includes notes issued for the purchase of the State Insurance Fund building.

## PROGRAMS AND FACILITIES OF THE AUTHORITY

### Office Buildings Program

Under its office buildings program, the Authority has completed construction of 203 office buildings (including police stations, courthouses and related facilities), amounting to 5,723,981 square feet of rentable space, for the use of and lease to various departments, agencies and instrumentalities of the Commonwealth. As of December 31, 1992, the estimated total cost of construction completed under the office building program was $315,000,000, which was provided principally by the Authority through the issuance of Revenue Bonds.

The Authority has under planning and construction one regional police headquarters, five police stations, and improvements to the central police headquarters and to a judicial center, at an estimated total cost of $35,000,000. All such office buildings have been or will be financed by Revenue Bonds, notes and internal funds.

### School Buildings Program

Under its school buildings program, the Authority has completed the construction of 238 school buildings, amounting to 8,627,304 square feet of rentable space, all of which has been leased to the Department of Education. As of December 31, 1992 the estimated total cost of construction completed under the school buildings program was $450,000,000, which was provided principally by the Authority through Public Education and Health Facilities Bonds. All completed facilities constructed under the Authority's school buildings program are leased to the Department of Education.

The Authority has under planning and construction 24 school buildings amounting to 1,199,591 square feet of rentable space to be leased to the Department of Education. The estimated total cost of construction of such school buildings is $93,000,000 to be financed through the issuance of Public Education and Health Facilities Bonds, notes and internal funds. The Authority is also considering the construction of additional school buildings to be leased to the Department of Education subject to various governmental and budgetary approvals, changing capital improvement priorities, variations in the economy, revenues available for capital expenditures, construction costs and other factors.

**Health Facilities Program**

Under its health facilities program, the Authority also has completed construction of 10 hospitals, 11 diagnostic and treatment centers and 8 family health centers, amounting to 3,295,006 square feet of rentable space, which has been leased to the Department of Health. As of December 31, 1992 the estimated total cost of construction completed under the program was $309,000,000 which was provided principally by the Authority through the issuance of Public Education and Health Facilities Bonds. All such completed facilities under the Authority's health facilities program are leased to the Department of Health.

The Authority has under planning and construction phases 3 hospitals and 7 health centers aggregating 708,639 square feet of rentable space, all to be leased to the Department of Health. The estimated total cost of construction of such facilities is $94,000,000 to be financed through the issuance of Public Education and Health Facilities Bonds, notes and the use of internal funds.

**Other**

In addition to the office buildings and school buildings and health facilities described above, the Authority has constructed 20 school buildings and 4 diagnostic and treatment centers at a cost of $50,633,716, which were financed by the U.S. Farmers Home Administration ("FmHA") and by the Authority's own resources. The amount financed by FmHA has been fully repaid.

Under the Enabling Act, the Authority is also empowered to construct social welfare facilities and correctional facilities. Any such facilities that may be constructed can be financed by bonds of the Authority under a bond resolution other than the 1970 or 1978 Bond Resolutions, and such bonds may be guaranteed by the Commonwealth under the Guaranty Act.

The Authority also constructs office buildings, schools and health facilities that are financed by a combination of Federal grants and Commonwealth appropriations. The Authority is also empowered to undertake construction on behalf of and as an agent for other public agencies of the Commonwealth.

## DEBT SERVICE REQUIREMENTS

Debt service requirements for the outstanding Revenue Bonds and Public Education and Health Facilities Bonds (excluding the Refunded Bonds), as shown in the following tables, consist in any fiscal year of the sum of the amounts required to pay (i) the interest that is payable on January 1 in such fiscal year and July 1 in the following fiscal year, (ii) the principal of serial bonds that is payable on July 1 in the following fiscal year, and (iii) the amortization requirements for term bonds for such fiscal year.

## REVENUE BONDS

| Fiscal Year Ending June 30 | Total Debt Service on Outstanding Revenue Bonds(1) | 1993 Revenue Refunding Bonds | | | | Total Debt Service |
|---|---|---|---|---|---|---|
| | | Serial Maturities | Amortization Requirements | Interest | Total | |
| | | | (in thousands) | | | |
| 1994 | $17,837 | | | $7,708(2) | $ 7,708 | $25,544 |
| 1995 | 17,834 | | | 7,115 | 7,115 | 24,948 |
| 1996 | 17,304 | | | 7,115 | 7,115 | 24,418 |
| 1997 | 17,303 | $1,460 | | 7,115 | 8,575 | 25,878 |
| 1998 | 17,968 | 2,140 | | 7,053 | 9,193 | 27,161 |
| 1999 | 15,604 | 4,605 | | 6,957 | 11,562 | 27,166 |
| 2000 | 18,151 | 2,325 | | 6,741 | 9,066 | 27,216 |
| 2001 | 18,152 | 2,450 | | 6,627 | 9,077 | 27,228 |
| 2002 | 16,149 | 2,590 | | 6,502 | 9,092 | 25,241 |
| 2003 | 14,741 | 2,135 | | 6,367 | 8,502 | 23,243 |
| 2004 | 14,738 | 2,250 | | 6,254 | 8,504 | 23,242 |
| 2005 | 4,574 | 2,375 | | 6,132 | 8,507 | 13,081 |
| 2006 | 4,569 | 2,500 | | 6,004 | 8,504 | 13,073 |
| 2007 | 2,054 | 5,120 | | 5,867 | 10,987 | 13,040 |
| 2008 | 2,052 | 5,400 | | 5,585 | 10,985 | 13,037 |
| 2009 | 2,045 | 5,735 | | 5,283 | 11,018 | 13,062 |
| 2010 | 2,042 | 6,065 | | 4,956 | 11,021 | 13,063 |
| 2011 | 2,039 | | $6,410 | 4,607 | 11,017 | 13,056 |
| 2012 | 2,041 | | 6,775 | 4,238 | 11,013 | 13,054 |
| 2013 | | | 7,170 | 3,849 | 11,019 | 11,019 |
| 2014 | | | 7,580 | 3,437 | 11,017 | 11,017 |
| 2015 | | | 8,015 | 3,001 | 11,016 | 11,016 |
| 2016 | | | 8,480 | 2,540 | 11,020 | 11,020 |
| 2017 | | | 8,965 | 2,052 | 11,017 | 11,017 |
| 2018 | | | 9,460 | 1,559 | 11,019 | 11,019 |
| 2019 | | | 9,985 | 1,039 | 11,024 | 11,024 |
| 2020 | | | 4,335 | 490 | 4,825 | 4,825 |
| 2021 | | | 4,570 | 251 | 4,821 | 4,821 |

(1) Does not include debt service requirements for the Refunded Revenue Bonds.

(2) Representing 13 months' interest.

## PUBLIC EDUCATION AND HEALTH FACILITIES BONDS

| Fiscal Year Ending June 30 | Total Debt Service on Outstanding Public Education and Health Facilities Bonds(1) | 1993 Public Education and Health Facilities Refunding Bonds | | | | Total Debt Service |
|---|---|---|---|---|---|---|
| | | Serial Maturities | Amortization Requirements | Interest | Total | |
| | | | (in thousands) | | | |
| 1994 | $47,291 | | | $34,832(2) | $34,832 | $82,123 |
| 1995 | 47,288 | | | 32,254 | 32,254 | 79,542 |
| 1996 | 44,063 | | | 32,254 | 32,254 | 76,317 |
| 1997 | 40,071 | | | 32,254 | 32,254 | 72,325 |
| 1998 | 37,030 | $ 4,485 | | 32,254 | 36,739 | 73,769 |
| 1999 | 32,728 | 21,890 | | 32,052 | 53,942 | 86,670 |
| 2000 | 37,343 | 18,330 | | 31,023 | 49,353 | 86,696 |
| 2001 | 37,335 | 19,235 | | 30,125 | 49,360 | 86,695 |
| 2002 | 37,301 | 20,250 | | 29,144 | 49,394 | 86,695 |
| 2003 | 33,831 | 24,775 | | 28,091 | 52,866 | 86,697 |
| 2004 | 25,977 | 17,960 | | 26,778 | 44,738 | 70,715 |
| 2005 | 17,227 | 22,780 | | 25,808 | 48,588 | 65,815 |
| 2006 | 17,212 | 24,030 | | 24,578 | 48,608 | 65,820 |
| 2007 | 12,597 | 30,000 | | 23,256 | 53,256 | 65,853 |
| 2008 | 12,572 | 31,640 | | 21,606 | 53,246 | 65,818 |
| 2009 | 12,558 | 33,430 | | 19,835 | 53,265 | 65,822 |
| 2010 | 12,538 | 35,355 | | 17,929 | 53,284 | 65,822 |
| 2011 | 12,512 | | $37,410 | 15,896 | 53,306 | 65,818 |
| 2012 | 12,481 | | 39,600 | 13,745 | 53,345 | 65,826 |
| 2013 | 794 | | 27,825 | 11,468 | 39,293 | 40,087 |
| 2014 | 794 | | 29,425 | 9,868 | 39,293 | 40,087 |
| 2015 | 794 | | 31,125 | 8,176 | 39,301 | 40,095 |
| 2016 | 794 | | 32,905 | 6,393 | 39,298 | 40,092 |
| 2017 | 16,679 | | 18,895 | 4,517 | 23,412 | 40,092 |
| 2018 | | | 19,935 | 3,478 | 23,413 | 23,413 |
| 2019 | | | 21,035 | 2,382 | 23,417 | 23,417 |
| 2020 | | | 10,835 | 1,225 | 12,060 | 12,060 |
| 2021 | | | 11,435 | 629 | 12,064 | 12,064 |

(1) Does not include debt service requirements for the Refunded Public Education and Health Facilities Bonds.

(2) Representing 13 months' interest.

## SUMMARY OF CERTAIN PROVISIONS OF THE 1970 BOND RESOLUTION

The following statements are brief summaries of certain provisions of the 1970 Bond Resolution. Such statements do not purport to be complete and reference is made to the 1970 Bond Resolution, copies of which are available for examination at the office of the 1970 Fiscal Agent. For the purposes of this summary, the terms "Bond" and "Bonds" shall refer to Revenue Bond or Bonds, as the case may be.

### Revenues

The Authority covenants that each lease agreement which it enters into for any office building financed under the 1970 Bond Resolution will require the lessee thereunder to pay rentals which in the aggregate will be sufficient to provide the sums needed from time to time (i) to pay the interest on all Bonds issued by the Authority for the financing of office buildings covered by such lease agreement, the principal of all such Bonds which are serial Bonds and the Amortization Requirements and redemption premium for any such Bonds which are term Bonds ("1970 Debt Service Rentals") and (ii) to pay the operating and maintenance expenses of such office buildings ("Operating Rentals"). (Section 701). All 1970 Debt Service Rentals and Operating Rentals received from the leasing of office buildings financed under the 1970 Bond Resolution are pledged as hereinafter provided.

### 1970 Sinking Fund

A special fund is created by the 1970 Bond Resolution and designated "Puerto Rico Public Buildings Authority Revenue Bonds Interest and Sinking Fund" (the "1970 Sinking Fund"). Three separate accounts are created in the 1970 Sinking Fund, namely the "1970 Bond Service Account", "1970 Redemption Account" and "1970 Reserve Account". (Section 502).

The Authority covenants that all 1970 Debt Service Rentals will be collected by the Authority and deposited with the 1970 Fiscal Agent to the credit of the following accounts in the following order:

(1) To the 1970 Bond Service Account, such amount thereof as may be required to make the amount then to the credit of the 1970 Bond Service Account equal to the amount of interest then due and payable and the interest which will become due and payable within the next ensuing six months on all Bonds of each Series then outstanding and the principal of all serial Bonds, if any, which will become payable within the next ensuing twelve months;

(2) To the 1970 Redemption Account, such amount as may be required to make the amounts so deposited in the then current fiscal year equal to the Amortization Requirement, if any, for such fiscal year for the term Bonds of each Series then outstanding, plus the premium, if any, which would be payable on a like principal amount of Bonds if such principal amount of Bonds should be redeemed on the next redemption date from moneys in the 1970 Sinking Fund; and

(3) The balance, if any, shall be deposited to the credit of the 1970 Reserve Account. (Section 502).

The requirements specified in paragraphs (1) and (2) above shall be cumulative. (Section 502).

The Authority covenants that all Operating Rentals received from the leasing of office buildings will be collected by the Authority and deposited as received with the Co-Fiscal Agent under the 1970 Bond Resolution to the credit of the Operating Fund. (Section 501).

#### *1970 Redemption Account*

Moneys in the 1970 Redemption Account shall be applied to the retirement of Bonds as follows:

(a) Subject to the provisions of paragraph (c) below, the 1970 Fiscal Agent shall endeavor to purchase outstanding Bonds, whether or not such Bonds shall then be subject to redemption, at the most advantageous price obtainable with reasonable diligence, having regard to interest rate and price, such price not to exceed the principal of such Bonds plus the amount of the premium, if any, which would be payable on the next redemption date to the holders of such Bonds if such Bonds should be called for redemption on such date from moneys in the 1970 Sinking Fund. The 1970 Fiscal Agent shall pay the interest accrued on such Bonds to the date of delivery thereof from the 1970 Bond Service Account and the purchase price from the 1970 Redemption Account, but no such purchase shall be made by the 1970 Fiscal Agent within 45 days next preceding any interest payment date on which such bonds are subject to call for redemption.

(b) Subject to the provisions of paragraph (c) below, the 1970 Fiscal Agent shall call for redemption on each date on which Bonds are subject to redemption from moneys in the 1970 Sinking Fund such amount of Bonds then subject to redemption as, with the redemption premium, if any, will exhaust the 1970 Redemption Account as nearly as may be; provided, however, that not less than $50,000 principal amount of Bonds shall be called for redemption at any one time. Not less than 30 days before the redemption date, the 1970 Fiscal Agent shall withdraw from the 1970 Bond Service Account and from the 1970 Redemption Account and set aside in separate accounts or deposit with the Paying Agents under the 1970 Bond Resolution the respective amounts required for paying the interest on, and the principal and redemption premium of, the Bonds so called for redemption.

(c) Moneys in the 1970 Redemption Account shall be applied to the purchase or redemption of Bonds in the following order:

*first,* term Bonds issued under the provisions of Section 207 of the 1970 Bond Resolution (including any term Bonds of the same Series issued under the provisions of Section 209 of the 1970 Bond Resolution), to the extent of the Amortization Requirement, if any, of the then current fiscal year for such term Bonds and any deficiency in preceding fiscal years in the purchase or redemption of such term Bonds;

*second,* term Bonds of each Series, if any, issued under the provisions of Section 208 of the 1970 Bond Resolution (including any term Bonds of the same Series issued under the provisions of Section 209 of the 1970 Bond Resolution) and term Bonds of each Series, if any, issued under the provisions of Section 210 of the 1970 Bond Resolution, in order of their issuance, to the extent of the Amortization Requirement, if any, of the then current fiscal year for such term Bonds and any deficiency in preceding fiscal years in the purchase or redemption of such term Bonds;

*third,* any balance then remaining shall be applied to the purchase or redemption of term Bonds of each such Series in proportion (as nearly as practicable) to the aggregate principal amount of the term Bonds of each such Series originally issued; and

*fourth,* after the retirement of all outstanding term Bonds, serial Bonds issued under any provisions of the 1970 Bond Resolution in the inverse order of their maturities, and to the extent that serial Bonds of different Series mature on the same date, in proportion (as nearly as practicable) to the principal amount of Bonds of each Series maturing on said date. (Section 504).

*1970 Reserve Account*

There shall be deposited by the Authority with the 1970 Fiscal Agent simultaneously with the delivery of any Bonds issued under the provisions of Section 208, Section 209 or Section 210 of the 1970 Bond Resolution, from Bond proceeds or other available moneys, to the credit of the 1970 Reserve Account such amount as may be required to make the balance therein equal to 50% of the maximum aggregate Principal and Interest Requirements in any fiscal year on account of all Bonds then outstanding, including the Bonds then to be issued. There may also be deposited to the credit of the 1970 Reserve Account at any time, in lieu of or substitution for such amounts, a Reserve Account Insurance Policy or Reserve Account Letter of Credit. Investments in the 1970 Reserve Account shall be valued at the lower of par and market value and Reserve Account Insurance Policies and Reserve Account Letters of Credit shall be valued at the amount then available thereunder. The term "Reserve Account Insurance Policy" shall mean an insurance policy, surety bond or other acceptable evidence of insurance, the issuer of which is a municipal bond insurer whose policy or bond results in the rating of municipal obligations secured by such policy or bond, at the time of deposit into the 1970 Reserve Account, in either of the two highest rating categories of either Moody's Investors Service, Inc. or any successors thereto or Standard & Poor's Corporation or any successors thereto. The term "Reserve Account Letter of Credit" shall mean an irrevocable, transferable letter of credit, the issuer of which is a banking association, bank or trust company or branch thereof whose letter of credit results in the rating of municipal obligations secured by such letter of credit, at the time of deposit into the 1970 Reserve Account, in either of the two highest rating categories of either Moody's Investors Service, Inc. or any successors thereto or Standard & Poor's Corporation or any successors thereto.

Moneys held in the 1970 Reserve Account shall first be used for the purpose of paying interest on the Bonds and maturing principal of serial Bonds whenever and to the extent that moneys held for the credit of the 1970 Bond Service Account shall be insufficient for such purpose and thereafter for the purpose of making the deposits to the credit of the 1970 Redemption Account mentioned in paragraph (2) above under the heading "1970 Sinking Fund" whenever and to the extent that the rentals of the Authority Buildings collected by the Authority are insufficient for such purpose. If at any time the moneys in the 1970 Reserve Account or amount available under any Reserve Account Insurance Policy or Reserve Account Letter of Credit shall exceed an amount equal to 50% of the maximum aggregate Principal and Interest Requirements in any fiscal year on account of all outstanding Bonds, such excess may be retained in the 1970 Reserve Account or may be applied to the payment of outstanding notes of the Authority or outstanding Bonds to be refunded pursuant to Section 210 of the 1970 Bond Resolution, or shall be deposited to the credit of the 1970 Construction Fund created under Article IV of the 1970 Bond Resolution or a special construction fund created pursuant to Section 209 of the 1970 Bond Resolution or the 1970 Redemption Account, at the option of the Authority; provided, however that any such excess arising from the deposit of a Reserve Account Insurance Policy or Reserve Account Letter of Credit shall be paid to the Authority. (Section 505).

If at any time amounts on deposit in the 1970 Reserve Account are used to pay any bond principal or interest as a result of the failure of any lessee of office buildings to pay the full amount of its 1970 Debt Service Rentals at the times required, or for any other reason, the Executive Director shall promptly file with the Secretary of the Treasury of the Commonwealth a notice of such failure or other reason which required such use of the amounts on deposit in the 1970 Reserve Account and request the Secretary of the Treasury to pay such 1970 Debt Service Rentals or to provide the funds otherwise required to reimburse the Authority for the amounts on deposit in the 1970 Reserve Account which were so used. (Section 505).

If at any time the amounts on deposit in the 1970 Reserve Account are used to pay any bond principal or interest as a result of the failure of any lessee of office buildings to pay the full amount of its 1970 Debt Service Rentals at the times required, the moneys thereafter received from the Secretary of the Treasury or from such delinquent lessees on account of such 1970 Debt Service Rentals shall be applied to the reimbursement of the moneys so withdrawn from the 1970 Reserve Account. (Section 505).

The term "Principal and Interest Requirement" for any fiscal year, as applied to the Bonds of any Series, shall mean the sum of:

(a) the amount required to pay the interest on all outstanding Bonds of such Series which is payable after July 1 in such fiscal year and on July 1 in the following fiscal year;

(b) the amount required to pay the principal of all outstanding serial Bonds of such Series which is payable after July 1 in such fiscal year and on July 1 in the following fiscal year; and

(c) the Amortization Requirement for the term Bonds of such Series for such fiscal year.

The following rules shall apply in determining the amount of the Principal and Interest Requirements for any period:

(i) in the case of Capital Appreciation Bonds, the Accreted Value thereof becoming due at maturity or by virtue of an Amortization Requirement shall be included when due and payable as part of the principal or Amortization Requirements in accordance with the above provisions;

(ii) in the case of Capital Appreciation and Income Bonds, the Appreciated Value thereof becoming due at maturity or by virtue of an Amortization Requirement shall be included when due and payable as part of principal or Amortization Requirements in accordance with the above provisions;

(iii) the interest rate on Bonds issued with a variable, adjustable, convertible or similar rate of interest shall be the average rate of interest on such Bonds for the preceding twelve months or such shorter period that such Bonds shall have been outstanding, or if such Bonds had not been outstanding prior to the date of calculation, the rate of interest on such Bonds on the date of calculation;

(iv) in the case of Bonds which by their terms may be tendered at the option of the holder thereof for payment prior to maturity, the tender date or dates shall be ignored if the tender price for such bonds is payable from a letter of credit or insurance policy or similar credit or liquidity facility and the stated dates for Amortization Requirements and principal payments shall be used; provided, however, that if the issuer of the letter of credit or insurance policy or similar credit or liquidity facility has advanced funds thereunder and such amount has not been repaid, Principal and Interest Requirements shall include the repayment obligations thereof in accordance with the principal repayment schedule and interest rate or rates specified in the letter of credit or insurance policy or similar credit or liquidity facility;

(v) in the case of Bonds the maturity of which may be extended at the option of the holder of the Bonds or the Authority, the Bonds shall be deemed to mature on the later of the stated maturity date or the date to which such stated maturity date has been extended; and

(vi) in the case of Bonds (A) which are expected to be repaid from the proceeds of Bonds or other indebtedness or (B) on which interest is payable periodically and for which twenty-five percent (25%) or more of the principal amount matures during any one year and for which no Amortization Requirements have been established, the debt service requirements on the Bonds may be excluded and in lieu thereof the Bonds shall be viewed, for purposes of the computation of Principal and Interest Requirements, as debt securities having a comparable federal tax status to that of the Bonds maturing in substantially equal annual payments of principal and interest over a period of thirty years from the date of issuance thereof, bearing interest at a fixed rate per annum equal to the average interest rate per annum for such debt securities on the date of issuance of the Bonds and issued by issuers having a credit rating, issued by Moody's Investors Service, Inc., or any successors thereto or Standard & Poor's Corporation or any successors thereto, comparable to that of the Authority, as shown by a certificate of an underwriting or investment banking firm experienced in marketing such securities.

**1970 Construction Fund**

The balance of the proceeds of each series of Bonds issued under the 1970 Bond Resolution available for payment of construction costs is required to be deposited with the Co-Fiscal Agent under the 1970 Bond Resolution to the credit of a special construction fund and applied to the payment of the cost of the Additional Public Office Buildings or Improvements for which such Bonds were issued. (Section 208).

Payments from these special construction funds are made upon requisition of the Authority signed by the Executive Director and the Treasurer and filed with the Co-Fiscal Agent under the 1970 Bond Resolution. (Sections 208 and 404). Any balance remaining in a special construction fund after the completion of such Buildings or Improvements for which the moneys in such fund were to be used shall be transferred by such Co-Fiscal Agent to the credit of the 1970 Reserve Account. (Section 408).

**Additional Bonds**

Additional Bonds may be issued from time to time to pay all or any part of the cost of any Additional Public Office Buildings or Improvements to any office buildings financed under the 1970 Bond Resolution or of any uncompleted part of the Additional Public Office Buildings or Improvements, to pay any notes of the Authority theretofore issued to finance such costs and to provide additional debt service reserves; provided that under the then existing law such Bonds may be specified by the Authority to be covered by the guaranty of the Commonwealth of Puerto Rico under the Guaranty Act and the Authority so specifies such Bonds by resolution. Before any such additional Bonds may be issued there must be filed with the 1970 Fiscal Agent, among other things, a certificate signed by the Executive Director of the Authority stating that on the basis of lease agreements entered into or which will be entered into by the Authority for such Buildings or for the buildings for which the Improvements are to be constructed, the 1970 Debt Service Rentals will be sufficient and timely to pay the principal of and interest on such Bonds. (Sections 208 and 209).

Refunding Bonds, including crossover refunding bonds, may be issued by the Authority at any time or times for the purpose of providing funds for refunding at or prior to their maturity or maturities all or any part of the outstanding Bonds of any Series, including the payment of any redemption premium thereon, and the interest which will accrue on such Bonds to the date fixed for redemption or maturity date or dates occurring prior thereto; provided that under the then existing law such Bonds may be specified by the Authority to be covered (as of the crossover date with respect to crossover refunding bonds) by the guaranty of the Commonwealth under the Guaranty Act and the Authority so specifies such refunding Bonds by resolution. (Section 102).

**Investment of Funds**

The 1970 Bond Resolution provides for the following types of investments:

(a) Government Obligations which are (i) direct obligations of, or obligations the principal of and the interest on which are unconditionally guaranteed by, the United States Government, (ii) bonds, debentures, notes or participation certificates issued by any of the following Federal agencies: Banks for Cooperatives, Federal Intermediate Credit Banks, Federal Home Loan Banks, Government National Mortgage Association or Federal Land Banks, (iii) obligations issued or guaranteed by an agency of the United States or person controlled or supervised by and acting as an instrumentality of the United States of America pursuant to authority granted by the Congress, (iv) evidences of direct ownership of proportionate interests in future interest or principal payments on obligations specified in clauses (i), (ii) and (iii) above held by a bank (including the 1970 Fiscal Agent) or trust company as custodian, under which the owner of the investment is the real party in interest and has the right to proceed directly and individually against the obligor on the underlying obligations described in said clauses (i), (ii) and (iii) and which underlying obligations are not available to satisfy any claim of the custodian or any person claiming through the custodian or to whom the custodian may be obligated, (v) municipal obligations, the payment of the principal of, interest and redemption premium, if any, on which are irrevocably secured by obligations described in clause (i) above and which obligations are not subject to redemption prior to the date on which the proceeds attributable to the principal of the obligations are to be used and have been deposited in an escrow account which is irrevocably pledged to the payment of the principal of and interest and redemption premium, if any, on such municipal obligations, and (vi) evidences of direct ownership of proportionate interests in future interest or principal payments on obligations specified in clause (v) above held by a bank (including the 1970 Fiscal Agent) or trust company as custodian, under which the owner of the investment is the real party in interest and has the right to proceed directly and individually against the obligor on the underlying obligations described in said clause (v) and which underlying obligations are not available to satisfy any claim of the custodian or any person claiming through the custodian or to whom the custodian may be obligated;

(b) Investment Obligations which are (i) Government Obligations, (ii) direct and general obligations of any state of the United States to the payment of the principal of and interest on which the full faith and credit of such state is pledged; provided that at the time of their purchase under the 1970 Bond Resolution such obligations are rated in either of the two highest rating categories by both Moody's Investors Service, Inc. or any successor thereto and Standard & Poor's Corporation or any successor thereto, (iii) New Housing Authority Bonds issued by public agencies of any state of the United States or municipalities in the United States and fully secured as to the payment of both principal and interest by a pledge of annual contributions under an annual contributions contract or contracts with the United States Government, (iv) Project Notes issued by public agencies of any state of the United States or municipalities in the United States and fully secured as to the payment of both principal and interest by a requisition or payment with the United States Government, and (v) any other investment obligations permitted under the laws of the Commonwealth of Puerto Rico which are rated, on the date of investment therein, or which are issued by issuers which are rated, on the date of investment therein, in any of the three highest rating categories by both Moody's Investors Service, Inc. or any successor thereto and Standard & Poor's Corporation or any successor thereto, or which are collateralized by such Investment Obligations; and

(c) Repurchase Agreements which are agreements between the 1970 Fiscal Agent and Government Development Bank for Puerto Rico ("GDB") or any bank or trust company (including the 1970 Fiscal Agent) which is a member of the Federal Deposit Insurance Corporation having a combined capital and surplus aggregating not less than $100,000,000, for the purchase of Government Obligations by the 1970 Fiscal Agent and for the repurchase of such Government Obligations on a specified date by such bank or trust company, such agreements to be secured by the Government Obligations so purchased. (Section 101).

Moneys held in the various Funds and Accounts shall (other than moneys held to the credit of the Operating Fund which shall only be invested in Government Obligations), as nearly as practicable, be invested and reinvested in Investment Obligations or Repurchase Agreements which shall mature, or which shall be subject to redemption by the holder thereof at the option of such holder:

(a) as to investments of moneys in the 1970 Bond Service Account, the 1970 Redemption Account and the 1970 Construction Fund, not later than the dates when the moneys held for the credit thereof will be required for the purposes intended,

(b) as to investments of moneys in the 1970 Reserve Account (i) 25% in principal amount, not later than the next interest payment date of Bonds issued under the 1970 Bond Resolution, (ii) 25% not later than the second interest payment date after such investment, and (iii) 50% not later than 3 years after the date of such investment, and

(c) as to investments of moneys in the Operating Fund, as specified by the Executive Director. (Section 602).

In lieu of such investments, moneys in any or all of such Funds or Accounts may be placed in interest bearing time deposits fully secured by Investment Obligations. (Section 602).

**General Covenants**

The Authority covenants that it will not agree to any amendment, modification or termination of any lease agreements which would reduce the amounts of rental payments below the amounts required by Section 701 of the 1970 Bond Resolution or postpone the times of making such rental payments or which would otherwise materially and adversely affect the security of the bondholders (Section 702), and that it will not create or suffer to be created any lien or charge upon the office buildings or upon the 1970 Debt Service Rentals or the Operating Rentals therefrom, other than the liens and charges created under the 1970 Bond Resolution. (Section 705).

The Authority covenants that it will cause annual audits to be made of its books and accounts relating to the office buildings by an independent firm of certified public accountants chosen by the Authority. Reports of such audits shall, among other things, set forth the findings of such certified public accountants as to whether the moneys received by the Authority under the 1970 Bond Resolution have been applied in accordance with the provisions thereof. Copies of such reports shall be filed with the 1970 Fiscal Agent and shall be mailed by the Authority to each bondholder who shall have filed his name and address with the Secretary of the Authority for such purpose. (Section 709).

**Modifications**

The Authority may adopt resolutions supplemental to the 1970 Bond Resolution without the consent of the bondholders to cure any ambiguity, formal defect or omission or to correct any inconsistent provisions or errors in the 1970 Bond Resolution, or to grant or confer upon the bondholders any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon the bondholders, or to add to the conditions, limitations and restrictions on the issuance of Bonds, or to add to the covenants and agreements of the Authority in the 1970 Bond Resolution or to surrender any right or power reserved to or conferred upon the Authority. (Section 901).

The holders of not less than two-thirds (⅔) in aggregate principal amount of the Bonds then outstanding shall have the right to consent to and approve the adoption of such resolution or resolutions supplemental to the 1970 Bond Resolution as shall be deemed necessary or desirable by the Authority for the purpose of modifying, altering, amending, adding to or rescinding any of the terms and provisions contained in the 1970 Bond Resolution; provided, however, that nothing contained in the 1970 Bond Resolution shall permit, or be construed as permitting, (a) an extension of the maturity of the principal of or the interest on any Bond, or (b) a reduction in the principal amount of any Bond or the redemption premium or the rate of interest thereon, or (c) the creation of a lien upon or a pledge of 1970 Debt Service Rentals or Operating Rentals other than the liens and pledges created by the 1970 Bond Resolution, or (d) a preference or priority of any Bond or Bonds over any other Bond or Bonds, or (e) a reduction in the aggregate principal amount of the Bonds required for consent to such supplemental resolution. (Section 902). No supplemental resolution may, however, change, amend or modify the rights or obligations of the 1970 Fiscal Agent or of any Paying Agent under the 1970 Bond Resolution without the written consent of the 1970 Fiscal Agent or such Paying Agent affected thereby. (Section 904).

### Notice of Default

In the event that the Authority shall default in the due and punctual performance of any covenants or agreements in the Bonds or the 1970 Bond Resolution and the 1970 Fiscal Agent shall have knowledge of, or is notified of, such default, and the Authority shall fail to correct such default within 30 days after notice thereof to the Authority by the 1970 Fiscal Agent, the 1970 Fiscal Agent shall promptly give notice of such default to the Secretary of the Treasury of the Commonwealth and GDB. (Section 804).

The 1970 Bond Resolution and the Bonds do not provide for acceleration of the maturities of the Bonds in the event of a default thereunder or in any other circumstances and do not provide that the bondholders may require the 1970 Fiscal Agent to take any action on their behalf.

### Commonwealth Guaranty

The Bonds will be specified to be guaranteed by the Commonwealth as provided in the Guaranty Act. See "Commonwealth Guaranty of the Bonds" under *Security*.

## SUMMARY OF CERTAIN PROVISIONS OF THE 1978 BOND RESOLUTION

The following statements are brief summaries of certain provisions of the 1978 Bond Resolution. Such statements do not purport to be complete and reference is made to the 1978 Bond Resolution, copies of which are available for examination at the office of the 1978 Fiscal Agent. For the purposes of this summary, the terms "Bond" or "Bonds" shall refer to the Public Education and Health Facilities Bond or Bonds.

### Revenues

The Authority covenants that each Lease Agreement which it enters into for any school or health or related facilities financed under the 1978 Bond Resolution ("Authority Facilities") will require the Lessee thereunder to pay annual rentals in substantially equal monthly installments which in the aggregate will be sufficient and timely to provide the sums needed from time to time (i) to pay the interest on all Bonds issued by the Authority for the financing of the Authority Facilities covered by such Lease Agreement, the principal of all such Bonds which are serial Bonds and the Amortization Requirements and redemption premium for any such Bonds which are term Bonds ("1978 Debt Service Rentals") and (ii) to provide and maintain in the 1978 Reserve Account in the 1978 Sinking Fund an amount with respect to all such Bonds equal to the greater of (A) 100% of the maximum aggregate annual interest on all such Bonds then outstanding or (B) 50% of the maximum aggregate Principal and Interest Requirements for any fiscal year on account of all such Bonds then outstanding ("Debt Service Reserve Rentals"). (Section 701). All 1978 Debt Service Rentals and Debt Service Reserve Rentals received from the leasing of Authority Facilities are pledged as hereinafter provided.

**1978 Sinking Fund**

A special fund is created by the 1978 Bond Resolution and designated "Puerto Rico Public Buildings Authority Public Education and Health Facilities Bonds Interest and Sinking Fund" (the "1978 Sinking Fund"). Three separate accounts are created in the 1978 Sinking Fund, namely, the "1978 Bond Service Account", "1978 Redemption Account" and "1978 Reserve Account", (Section 501).

The Authority covenants that all 1978 Debt Service Rentals will be collected by the Authority and immediately deposited with the 1978 Fiscal Agent to the credit of the following Accounts in the following order:

(1) To the 1978 Bond Service Account, such amount thereof as may be required to make the amount then to the credit of the 1978 Bond Service Account equal to the amount of interest then due and payable and the interest which will accrue up to the next interest payment date on all Bonds of each Series then outstanding and the principal of all serial Bonds, if any, which will become due and payable within the next ensuing twelve months;

(2) To the 1978 Redemption Account, such amount of the balance remaining after making the deposit under paragraph (1) above as may be required to make the amounts so deposited in the then current fiscal year equal to the Amortization Requirement, if any, for such fiscal year for the term Bonds of each Series then outstanding, plus the premium, if any, which would be payable on a like principal amount of Bonds if such principal amount of Bonds should be redeemed on the next redemption date from moneys in the 1978 Sinking Fund; and

(3) The balance, if any, shall be deposited to the credit of the 1978 Reserve Account. (Section 501).

The requirements specified in paragraphs (1) and (2) above shall be cumulative. (Section 501).

The Authority covenants that all Debt Service Reserve Rentals received from the leasing of Authority Facilities will be collected by the Authority and immediately deposited with the 1978 Fiscal Agent to the credit of the 1978 Reserve Account. (Section 501).

*1978 Redemption Account*

Moneys in the 1978 Redemption Account shall be applied to the retirement of Bonds as follows:

(a) Subject to the provisions of paragraph (c) below, the 1978 Fiscal Agent shall endeavor to purchase outstanding Bonds, whether or not such Bonds shall then be subject to redemption, at the most advantageous price obtainable with reasonable diligence, having regard to interest rate and price, such price not to exceed the principal of such Bonds plus the amount of the premium, if any, which would be payable on the next redemption date to the holders of such Bonds if such Bonds should be called for redemption on such date from moneys in the 1978 Sinking Fund. The 1978 Fiscal Agent shall pay the interest accrued on such Bonds to the date of delivery thereof from the 1978 Bond Service Account and the purchase price from the 1978 Redemption Account, but no such purchase shall be contracted for within 45 days next preceding any interest payment date on which such Bonds are subject to call for redemption.

(b) Subject to the provisions of paragraph (c) below, the 1978 Fiscal Agent shall call for redemption on each date on which Bonds are subject to redemption from moneys which are in the 1978 Sinking Fund on the forty-fifth day prior to such redemption date such amount of Bonds then subject to redemption as, with the redemption premium, if any, will exhaust the 1978 Redemption Account as nearly as may be; provided, however, that not less than $50,000 principal amount of Bonds shall be called for redemption at any one time. Not less than 30 days before the redemption date the 1978 Fiscal Agent shall withdraw from the 1978 Bond Service Account and from the 1978 Redemption Account and set aside in separate accounts or deposit with the Paying Agents under the 1978 Bond Resolution the respective amounts required for paying the interest on, and the principal of and redemption premium on, the Bonds so called for redemption.

(c) Moneys in the 1978 Redemption Account shall be applied by the 1978 Fiscal Agent in each fiscal year to the purchase or redemption of Bonds of each Series then outstanding in the following order:

*first,* term Bonds of each Series to the extent of the Amortization Requirement, if any, for such fiscal year for such term Bonds of each such Series then outstanding plus the applicable premium, if any;

*second,* any balance then remaining shall be applied to the purchase of any Bonds whether or not such Bonds shall be subject to redemption in accordance with paragraph (a) above;

*third,* any balance then remaining shall be applied to the redemption of term Bonds of each Series in proportion to the Amortization Requirement, if any, for such fiscal year for the term Bonds of each such Series then outstanding plus the applicable premium, if any; and

*fourth,* after the retirement of all term Bonds, any balance still remaining shall be applied to the retirement of the serial Bonds of each Series in proportion to the aggregate principal amount of the serial Bonds of such Series originally issued. (Section 503).

*1978 Reserve Account*

The Authority may deposit in the 1978 Reserve Account, a Reserve Account Insurance Policy or a Reserve Account Letter of Credit in lieu of or in substitution for moneys or securities on deposit in the 1978 Reserve Account. (Section 501). The Reserve Account Insurance Policy and the Reserve Account Letter of Credit are defined as follows:

The term "Reserve Account Insurance Policy" shall mean the insurance policy, surety bond or other acceptable evidence of insurance, if any, deposited in the 1978 Reserve Account in lieu of or in partial substitution for cash or securities on deposit therein. The issuer providing such insurance shall be a municipal bond insurer whose policy or bond results in the rating of municipal obligations secured by such policy or bond to be rated, at the time of deposit into the 1978 Reserve Account, in either of the two highest rating categories of either Moody's Investors Service, Inc. or any successors thereto or Standard & Poor's Corporation or any successors thereto.

"Reserve Account Letter of Credit" shall mean the irrevocable, transferable letter of credit, if any, deposited in the 1978 Reserve Account in lieu of or in partial substitution for cash or securities on deposit therein. The issuer providing such letter of credit shall be a banking association, bank or trust company or branch thereof whose letter of credit results in the rating of municipal obligations secured by such letter of credit to be rated, at the time of deposit into the Reserve Account, in either of the two highest rating categories of either Moody's Investors Service, Inc. or any successors thereto or Standard & Poor's Corporation or any successors thereto. (Section 101).

Moneys held in the 1978 Reserve Account or amounts available under any Reserve Account Insurance Policy or Reserve Account Letter of Credit shall first be used for the purpose of paying interest on the Bonds and maturing principal of serial Bonds whenever and to the extent that moneys held for the credit of the 1978 Bond Service Account shall be insufficient for such purpose, and thereafter for the purpose of making the deposits to the credit of the 1978 Redemption Account mentioned in paragraph (2) above under the heading "1978 Sinking Fund" whenever and to the extent that the 1978 Debt Service Rentals of the Authority Facilities collected by the Authority are insufficient for such purpose. If at any time moneys in the 1978 Reserve Account or amounts available under any Reserve Account Insurance Policy or Reserve Account Letter of Credit shall exceed an amount equal to the greater of (a) 100% of the maximum aggregate annual interest on all bonds then outstanding or (b) 50% of the maximum aggregate Principal and Interest Requirements for any fiscal year on account of all Bonds then outstanding, such excess may be retained in the 1978 Reserve Account, may be applied to the payment of outstanding notes issued by the Authority to finance temporarily any school and health facilities or outstanding Bonds to be refunded pursuant to Section 209 of the 1978 Bond Resolution, or may be deposited to the credit of the 1978 Bond Service Account, the 1978 Redemption Account or the 1978 Construction Fund (hereinafter mentioned) or any Reserve Account

Insurance Policy or Reserve Account Letter of Credit may be reduced to the extent of such excess, at the option of the Authority. (Section 504).

If at any time amounts on deposit in the 1978 Reserve Account are used to pay the principal, or redemption premium or interest on, any Bond as a result of the failure of a Lessee to pay the full amount of its 1978 Debt Service Rentals at the times required, or for any other reason, the Executive Director of the Authority shall promptly file with the Secretary of the Treasury of the Commonwealth a notice of such failure or other reason which required such use of the amounts on deposit in the 1978 Reserve Account and request the Secretary of the Treasury to pay such 1978 Debt Service Rentals or to provide the funds otherwise required to reimburse the Authority for the amounts on deposit in the 1978 Reserve Account which were so used. If at any time the amount on deposit to the credit of the 1978 Reserve Account is not equal to the greater of (a) 100% of the maximum aggregate annual interest on all Bonds then outstanding or (b) 50% of the maximum aggregate Principal and Interest Requirements for any fiscal year on account of all Bonds then outstanding, other than because of the use of the moneys as referred to in the preceding sentence in this paragraph, the Executive Director of the Authority shall promptly notify the Lessees that Debt Service Reserve Rentals under the Lease Agreements in an aggregate amount sufficient to make the amount then on deposit to the credit of the 1978 Reserve Account equal to the greater of 100% of such maximum annual interest or 50% of such maximum Principal and Interest Requirements shall be due and payable under the Lease Agreements within 30 days after the giving of such notice to the Lessees. In the event of a failure of a Lessee to pay such Debt Service Reserve Rentals as aforesaid, the Executive Director of the Authority shall promptly request the Secretary of the Treasury of the Commonwealth to pay such unpaid Debt Service Reserve Rentals. The moneys thereafter received from the Secretary of the Treasury or from the Lessees on account of such Debt Service Rentals or Debt Service Reserve Rentals or other required funds shall be deposited to the credit of the 1978 Reserve Account. Concurrently with the filing or giving of any notice or request as provided in this paragraph, copies thereof shall be sent by the Executive Director of the Authority, to the 1978 Fiscal Agent and to Government Development Bank. (Section 504).

The term "Principal and Interest Requirement" for any fiscal year, as applied to the Bonds of any Series under the 1978 Resolution, shall mean the sum of:

(a) the amount required to pay the interest on all outstanding Bonds of such Series which is payable during such fiscal year, and, in the case of Bonds issued with January 1 and July 1 interest payment dates, is payable on January 1 in such fiscal year and on July 1 in the following fiscal year;

(b) the amount required to pay the principal of all outstanding serial Bonds of such Series during such fiscal year, and, in the case of Bonds on which principal is payable on July 1, the principal which is payable on July 1 in the following fiscal year; and

(c) the Amortization Requirement for the term Bonds of such Series for such fiscal year.

The following rules shall apply in determining the amount of the Principal and Interest Requirements for any period:

(i) in the case of Capital Appreciation Bonds, the Accreted Value of Capital Appreciation Bonds becoming due at maturity or by virtue of an Amortization Requirement shall be included when due and payable as part of the principal or Amortization Requirements in accordance with the above provisions;

(ii) in the case of Capital Appreciation and Income Bonds, the Appreciated Value of Capital Appreciation and Income Bonds becoming due at maturity or by virtue of an Amortization Requirement shall be included when due and payable as part of principal or Amortization Requirements in accordance with the above provisions;

(iii) the interest rate on bonds issued with a variable, adjustable, convertible or similar rates of interest shall be the average rate of interest per annum for the preceding twelve months or such shorter period that such bonds shall have been outstanding, or if such bonds had not been outstanding prior to the date of calculation, the rate of interest on such bonds on the date of calculation;

(iv) in the case of Bonds which by their terms may be tendered by and at the option of the holder thereof for payment prior to maturity, the tender date or dates shall be ignored if the tender price for such bonds is payable from a letter of credit or insurance policy or similar credit or liquidity facility and the stated dates for Amortization Requirements and principal payments shall be used; provided, however, that if the issuer of the letter of credit or insurance policy or similar credit or liquidity facility has advanced funds thereunder and such amount has not been repaid, Principal and Interest Requirements shall include the repayment obligations thereof in accordance with the principal repayment schedule and interest rate or rates specified in the letter of credit or insurance policy or similar credit or liquidity facility;

(v) in the case of Bonds the maturity of which may be extended by and at the option of the holder of the Bonds or the Authority, the Bonds shall be deemed to mature on the later of the stated maturity date or the date to which such stated maturity date has been extended; and

(vi) in the case of Bonds (A) which are expected to be repaid from the proceeds of Bonds or other indebtedness or (B) on which interest is payable periodically and for which twenty-five percent (25%) or more of the principal amount matures during any one year and for which no Amortization Requirements have been established, the debt service requirements on the Bonds may be excluded and in lieu thereof the Bonds shall be viewed, for purposes of the computation of Principal and Interest Requirements, as debt securities having a comparable federal tax status to that of the bonds, maturing in substantially equal annual payments of principal and interest over a period of thirty years from the date of issuance thereof, bearing interest at a fixed rate per annum equal to the average interest rate per annum for such debt securities on the date of issuance of the Bonds and issued by issuers having a credit rating, issued by Moody's Investors Service, Inc., or any successors thereto or Standard & Poor's Corporation or any successors thereto, comparable to that of the Authority, as shown by a certificate of an underwriting or investment banking firm experienced in marketing such securities.

**1978 Construction Fund**

The balance of proceeds of Bonds issued under Section 208 of the 1978 Bond Resolution available for payment of construction costs is required to be deposited with the 1978 Fiscal Agent to the credit of the Construction Fund under the 1978 Bond Resolution (the "1978 Construction Fund") and applied to the payment of the cost of the Additional Facilities or Improvements for which such Bonds were issued. (Section 208).

Payments from the 1978 construction Fund are made upon requisition of the Authority signed by the Executive Director and by one or more officer or employee of the Authority designated by the Executive Director certifying that the moneys to be disbursed will be applied to the cost of Authority facilities and filed with the 1978 Fiscal Agent. (Section 404). Any balance remaining in the 1978 Construction Fund from time to time after the completion of the Authority Facilities and Improvements theretofore financed by the Authority may at the direction of the Authority be transferred by the 1978 Fiscal Agent to the credit of the 1978 Reserve Account. (Section 406).

**Additional Bonds**

Additional Bonds may be issued from time to time to provide funds to pay all or any part of any remaining costs of the Initial Facilities or to pay all or any part of the cost of any Additional Facilities or Improvements to Authority Facilities financed under the 1978 Bond Resolution or of any uncompleted part of the Initial Facilities or Additional Facilities or improvements, to pay any notes of the Authority theretofore issued to finance such costs, and to provide additional debt service reserves; provided that under the then existing law such Bonds may be specified by the Authority to be covered by the guaranty of the Commonwealth of Puerto Rico under the Guaranty Act and the Authority so specifies such Bonds by resolution. Before any such additional Bonds may be issued there must be filed with the 1978 Fiscal Agent, among other things, a certificate signed by the Executive Director of the Authority starting that on the basis of all Lease Agreements or amendments or supplements thereto, the 1978 Debt Service Rentals, as calculated by the Authority, will be sufficient and timely to pay the principal of, and the redemption premium, if any, and interest on, such Bonds and all Bonds then outstanding. (Section 208).

Refunding Bonds, including crossover refunding bonds, may be issued by the Authority at any time or times for the purpose of providing funds for refunding at or prior to their maturity or maturities all or any part of the outstanding Bonds of any Series, including the payment of any redemption premium thereon and interest which will accrue on such Bonds to the redemption date or maturity date or dates occurring prior thereto; provided that under the then existing law such Bonds may be specified by the Authority to be covered (as of the crossover date with respect to crossover refunding bonds) by the guaranty of the Commonwealth under the Guaranty Act and the Authority so specifies such refunding bonds by resolution. (Section 209).

**Investment of Funds**

The 1978 Bond Resolution provides for the following types of investments:

(a) Government Obligations which are (i) direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by, the United States Government, (ii) bonds, debentures or notes issued by any of the following Federal agencies: Banks for Cooperatives, Federal Intermediate Credit Banks, Federal Home Loan Banks, Export-Import Bank of the United States, Government National Mortgage Association or Federal Land Banks, (iii) obligations issued or guaranteed by an agency of the United States of America or person controlled or supervised by and acting as an instrumentality of the United States of America pursuant to authority granted by the Congress, (iv) municipal obligations, the payment of the principal of, interest and redemption premium, if any, on which are irrevocably secured by obligations described in clause (i) above and which obligations are not subject to redemption prior to the date on which the proceeds attributable to the principal of the obligations are to be used and have been deposited in an escrow account which is irrevocably pledged to the payment of the principal of and interest and redemption premium, if any, on such municipal obligations, and (v) evidences of ownership of proportionate interests in future interest or principal payments on obligations specified in clauses (i), (ii), (iii) and (iv) above held by a bank (including the 1978 Fiscal Agent) or trust company as custodian and which underlying obligations are not available to satisfy any claim of the custodian or any person claiming through the custodian or to whom the custodian may be obligated.

(b) Investment Obligations which are (i) Government Obligations, (ii) direct and general obligations of any state of the United States to the payment of the principal of and interest on which the full faith and credit of such state is pledged; provided that such obligations are rated, on the date of investment therein in either of the two highest rating categories by Moody's Investors Service, Inc. or any successors thereto and Standard & Poor's Corporation or any successors thereto, (iii) New Housing Authority Bonds issued by public agencies of any state of the United States or municipalities in the United States and fully secured as to the payment of both principal and interest by a pledge of annual contributions under an annual contributions contract or contracts with the United States Government, (iv) Project Notes issued by public agencies of any state of the United States or municipalities in the United States and fully secured as to the payment of both principal and interest by a requisition or payment agreement with the United States Government, and (v) any other investment obligations permitted under the laws of the Commonwealth of Puerto Rico which are rated, on the date of investment therein, or which are issued by issuers which are rated, on the date of investment therein, in any of the three highest rating categories by Moody's Investors Service, Inc. or any successors thereto and Standard & Poor's Corporation or any successors thereto, or which are collateralized by such Investment Obligations;

(c) Repurchase Agreements which are agreements between the 1978 Fiscal Agent and GDB or any bank or trust company (including the 1978 Fiscal Agent) which is a member of the Federal Deposit Insurance Corporation having a combined capital and surplus aggregating not less than $100,000,000, for the purchase of Government Obligations by the 1978 Fiscal Agent and for the repurchase of such Government Obligations on a specified date by such bank or trust company, such agreements to be secured by the Government Obligations so purchased; and

(d) Time Deposits which are time deposits, certificates of deposit or other similar arrangements with the 1978 Fiscal Agent, GDB or any bank or trust company which is a member of the Federal Deposit Insurance Corporation having a combined capital and surplus aggregating not less than $100,000,000. (Section 101).

Moneys held in the 1978 Construction Fund, the 1978 Bond Service Account, the 1978 Redemption Account and the 1978 Reserve Account shall, as nearly as practicable, be invested and reinvested in Investment Obligations, Repurchase Agreements, or Time Deposits fully secured by Investment Obligations, which mature, or are subject to redemption by the holder thereof at the option of such holder:

(a) as to investments of moneys in the 1978 Bond Service Account, the 1978 Redemption Account and the 1978 Construction Fund, not later than the dates when the moneys held for the credit thereof will be required for the purposes intended, and

(b) as to investments of moneys in the 1978 Reserve Account (i) 50% in principal amount, not later than five years from the date of such investment and (ii) the balance as specified by the Executive Director of the Authority. (Section 602).

**General Covenants**

The Authority covenants that it will not agree to any amendment, modification or termination of any Lease Agreements which would reduce the amounts of rental payments below the amounts required by Section 701 of the 1978 Bond Resolution or postpone the times of making such rental payments or which would otherwise materially and adversely affect the security of the bondholders (Section 702), that it will not create or suffer to be created any lien or charge upon the Authority Facilities or upon the 1978 Debt Service Rentals or Debt Service Reserve Rentals therefrom, other than the liens and charges created under the 1978 Bond Resolution (Section 705), and that each Lease Agreement will provide that the obligation of the Lessee to pay timely the required rentals thereunder shall be absolute and unconditional. (Section 709).

The Authority covenants that it will cause audits to be made of its books and accounts by an independent firm of certified public accountants chosen by the Authority. Reports of such audits shall, among other things, set forth the findings of such certified public accountants as to whether the moneys received by the Authority under the 1978 Bond Resolution have been applied in accordance with the provisions thereof. Copies of such reports shall be filed with the 1978 Fiscal Agent and shall be mailed by the Authority to each bondholder who shall have filed his name and address with the Secretary of the Authority for such purpose. (Section 712).

**Modifications**

The Authority may adopt resolutions supplemental to the 1978 Bond Resolution without the consent of the bondholders to cure any ambiguity, formal defect or omission or to correct any inconsistent provisions or errors in the 1978 Bond Resolution; provided such action shall not adversely affect the interests of the bondholders, or to grant or confer upon the bondholders any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon the bondholders, or to add to the conditions, limitations and restrictions on the issuance of Bonds, or to add to the covenants and agreements of the Authority in the 1978 Bond Resolution or to surrender any right or power reserved to or conferred upon the Authority. (Section 901).

The holders of not less than two-thirds (⅔) in aggregate principal amount of the Bonds then outstanding shall have the right to consent to and approve the adoption of such resolution or resolutions supplemental to the 1978 Bond Resolution as shall be deemed necessary or desirable by the Authority for the purpose of modifying, altering, amending, adding to or rescinding any of the terms and provisions contained in the 1978 Bond Resolution; provided, however, that nothing contained in the 1978 Bond Resolution shall permit, or be construed as permitting, (a) an extension of the maturity of the principal of or the interest on any Bond, or (b) a reduction in the principal amount of any Bond or the redemption premium or the rate of interest thereon, or (c) the creation of a lien upon or a pledge of 1978 Debt Service Rentals or Debt Service Reserve Rentals other than the liens and pledges created by or pursuant to the 1978 Bond Resolution, or (d) a preference or priority of any Bond or Bonds over any other Bond or Bonds, or (e) a reduction in the aggregate principal amount of the Bonds required for consent to such supplemental resolution. (Section 902). No supplemental resolution may, however, change, amend or modify the rights or obligations of the 1978 Fiscal Agent or of any Paying Agent under the 1978 Bond Resolution without the written consent of the 1978 Fiscal Agent or such Paying Agent affected thereby. (Section 904).

### Notice of Default

In the event that on the second business day prior to the date on which a payment of interest, principal, or premium, if any, is due on any Bond there is not an amount sufficient in such account or fund as the 1978 Fiscal Agent may draw upon for the payment on such due date of such interest, principal, or premium, or the Authority shall default in the due and punctual making of any 1978 Sinking Fund deposit required by Section 501 of the 1978 Bond Resolution, the 1978 Fiscal Agent shall promptly give written notice of such insufficiency or default, as the case may be, to the Authority, the Secretary of the Treasury of the Commonwealth and GDB. In the event that the Authority shall default in the due and punctual performance of any other covenants or agreements in the Bonds or the 1978 Bond Resolution and the 1978 Fiscal Agent shall have knowledge of, or is notified of, such default, and the Authority shall fail to correct such default within 30 days after notice thereof to the Authority by the 1978 Fiscal Agent, the 1978 Fiscal Agent shall promptly give notice of such default to the Secretary of the Treasury of the Commonwealth and GDB. (Section 804).

The 1978 Bond Resolution and the Bonds do not provide for acceleration of the maturities of the Bonds in the event of a default thereunder or in any other circumstances and do not provide that the bondholders may require the 1978 Fiscal Agents to take any action on their behalf.

### Commonwealth Guaranty

The Bonds will be specified to be guaranteed by the Commonwealth as provided in the Guaranty Act. See "Commonwealth Guaranty of the Bonds" under *Security*.

## TAX EXEMPTION

The Internal Revenue Code of 1986, as amended (the "Code"), includes requirements which the Authority must continue to meet after the issuance of the Bonds in order that interest on the Bonds not be included in gross income for federal income tax purposes. The Authority's failure to meet these requirements may cause interest on the Bonds to be included in gross income for federal income tax purposes retroactive to their date of issuance. The Authority has covenanted in the resolutions adopted in connection with the issuance of the Bonds to comply to the extent permitted by the Constitution and the laws of the Commonwealth with the requirements of the Code in order to maintain the exclusion from gross income for federal income tax purposes of interest on the Bonds. Bond Counsel is aware of no provision of the Constitution or laws of the Commonwealth which would prevent the Authority from complying with the requirements of the Code.

In the opinion of Bond Counsel, subject to continuing compliance by the Authority with the tax covenant referred to above, under existing statutes, regulations, rulings and court decisions, interest on the Bonds is not includable in gross income for federal income tax purposes. Interest on the Bonds is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, interest on the Bonds will be includable in the computation of the alternative minimum tax and the environmental tax on corporations imposed by the Code. Bond Counsel is further of the opinion that the Bonds and the interest thereon are exempt from state, Commonwealth and local income taxation.

Ownership of tax-exempt obligations may result in collateral federal income tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, certain foreign corporations, certain S Corporations with excess passive income, individual recipients of Social Security or Railroad Retirement benefits and taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations. Companies which qualify for and which have elected the benefits of Section 936 of the Code should consult their tax advisors as to whether interest on the Bonds constitutes income eligible for the credit provided by Section 936 of the Code.

Ownership of tax-exempt obligations may also result in collateral income tax consequences under Puerto Rico law to financial institutions doing business in Puerto Rico.

Prospective purchasers of the Bonds should consult their tax advisors as to applicability and impact of any collateral consequences.

## DISCOUNT BONDS

Under the Code, the difference between the principal amount of the Bonds including the TXCs (other than the Bonds maturing July 1, 2010 and the 1993 Public Education and Health Facilities Refunding Bonds maturing July 1, 2016) (collectively, the "Discount Bonds"), and the initial offering price to the public (excluding bond houses and brokers) at which price a substantial amount of such Discount Bonds of the same series and maturity was sold is original issue discount. Original issue discount on the Discount Bonds represents interest which is not includable in federal gross income. A portion of such interest that accrues to the Beneficial Owner of such Discount Bonds in each year, as described below, is, however, included in the calculation for determining a corporate taxpayer's alternative minimum tax and environmental tax and the distribution requirements of certain regulated investment companies and may result in some of the collateral federal income tax consequences described above under the caption "Tax Exemption" in the year of accrual. Consequently, Beneficial Owners of Discount Bonds should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability, environmental tax liability, additional distribution requirements or other collateral federal income tax consequences although the Beneficial Owner may not have received cash in such year. Original issue discount on Discount Bonds will accrue over the terms of such Bonds at a constant interest rate compounded in a manner similar to that used in computing accreted values on capital appreciation bonds. A purchaser in the initial offering who acquires a Discount Bond at an issue price equal to the initial offering price thereof as set forth or derived from information set forth on the inside cover page hereof will be treated as receiving an amount of interest not includable in gross income for federal income tax purposes equal to the original issue discount accruing during the period he holds such Discount Bond and will increase his adjusted basis in such Discount Bond by the amount of such accruing discount for purposes of determining taxable gain or loss on the sale or other disposition of such Discount Bond. Purchasers of TXCs should consult their tax advisors as to the tax consequences of converting PTXCs to other combinations of TXCs and selling any portion of the TXCs so converted in the secondary market. A purchaser of any portion of a TXC in the secondary market from a purchaser in the initial offering may treat a portion of any discount as original issue discount to the extent such discount does not produce a yield to maturity of the purchased portion of the TXC as of the purchase date which exceeds the lesser of (a) either, at the election of the purchaser, the coupon rate of interest or the original yield to maturity on the obligation from which the coupons were separated (5.575% in respect of TXCs relating to 1993 TXC Bonds maturing July 1, 2007 and 5.625% in respect of TXCs relating to 1993 TXC Bonds maturing July 1, 2008) and (b) the yield to maturity (on the basis of purchase price) of the purchased TXC. The federal income tax consequences of the purchase, ownership and redemption, sale or other disposition of Discount Bonds which are not purchased in the initial offering at the initial offering price may be determined according to rules which differ from those described above. Beneficial Owners of Discount Bonds including the TXCs should consult their tax advisors with respect to the precise determination for federal income tax purposes of interest accrued upon sale, redemption or other disposition of Discount Bonds including the TXCs and with respect to the state and local tax consequences of owning and disposing of Discount Bonds including the TXCs.

## VERIFICATION OF MATHEMATICAL COMPUTATIONS

The arithmetical accuracy of (a) the mathematical computations of the adequacy of the outstanding maturing amount of and interest on the direct obligations of the United States of America plus other available moneys remaining uninvested to pay the redemption prices of the Refunded Bonds on their respective redemption dates, together with all payments of interest thereon coming due prior to such dates (see *Plan of Financing*) and (b) the mathematical computations supporting the conclusion of Bond Counsel that the Bonds are not "arbitrage bonds" under Section 148 of the Code, will be verified by Ernst & Young, independent certified public accountants.

## UNDERWRITING

The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the Bonds from the Authority at an aggregate discount of $6,220,851.76 from the initial public offering prices set forth or derived from information set forth on the cover or inside cover page. The Underwriters' obligations are subject to certain conditions precedent, and they will be obligated to purchase all the Bonds if any are purchased. The Bonds may be offered and sold to certain dealers (including dealers depositing such Bonds into investment trusts) at prices lower than such public offering prices, and such public offering prices may be changed from time to time by the Underwriters. The Authority has agreed to indemnify, to the extent permitted by law, the Underwriters against certain liabilities, including liabilities under Federal securities laws.

## LEGAL INVESTMENT

The Bonds will be eligible for deposit by banks in Puerto Rico to secure public funds and will be approved investments for insurance companies to qualify them to do business in Puerto Rico as required by law.

## LEGAL MATTERS

The proposed forms of opinions of Brown & Wood, New York, New York, Bond Counsel, are set forth in Appendices IV and V. Certain legal matters will be passed upon for the Underwriters by their counsel, Rogers & Wells, New York, New York.

## GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

As required by Act No. 272 of the Legislature of Puerto Rico, approved May 15, 1945, as amended, GDB has acted as financial advisor to the Authority in connection with the Bonds offered hereby.

## RATINGS

Moody's Investors Service, Inc. and Standard & Poor's Corporation have given the Bonds ratings of Baa1 and A, respectively. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained only from the respective rating agency.

Such rating agencies were provided with materials relating to the Authority, the Commonwealth, the Bonds and other relevant information. No application has been made to any other rating agency for the purpose of obtaining a rating on the Bonds.

There is no assurance that any ratings obtained will remain in effect for any given period of time or that they will not be revised downward or withdrawn entirely by either or both of such rating agencies if, in the judgment of either or both, circumstances so warrant. Any such downward revision or withdrawal of such ratings, or either of them, may have an adverse effect on the market prices of the Bonds.

## MISCELLANEOUS

The foregoing references to and summaries of certain provisions of the 1970 Bond Resolution, the 1978 Bond Resolution, the lease agreements with respect to the facilities that are to be financed in whole or in part by the Bonds, the various acts and the Bonds are made subject to all the detailed provisions thereof, to which reference is hereby made for further information, and do not purport to be complete statements of any or all of such provisions.

Appended to, and constituting a part of, this Official Statement is certain information concerning the Commonwealth, the general purpose financial statements of the Commonwealth for the year ended June 30, 1991, together with the report of KPMG Peat Marwick, the financial statements of the Authority for the years ended June 30, 1992 and 1991, together with the report of Coopers & Lybrand, the proposed forms of opinions of Brown & Wood, Bond Counsel and information concerning the TXCs and Indexed Inverse Floaters.

The financial statements of the Authority included in Appendix III have been audited by Coopers & Lybrand, San Juan, Puerto Rico, as set forth in their report therein. The information set forth in *Provisions Relating to Public Debt of the Commonwealth* in Appendix I and Appendix II was supplied by certain officials of the Commonwealth or certain of its agencies or instrumentalities, in their respective official capacities, or was obtained from publications of the Commonwealth or certain of its agencies or instrumentalities, and is included in this Official Statement on the authority of such officials or the authority of such publications as public official documents, respectively. The information set forth in this Official Statement, except the information appearing in *Provisions Relating to Public Debt of the Commonwealth, Underwriting* and "Book Entry Only System" under *Description of the Bonds,* and in Appendices I, II, III, IV, V, VI and VII, was supplied by the Executive Director of the Authority in his official capacity as such Executive Director and is included in this Official Statement on his authority. The information pertaining to DTC was supplied by DTC.

The Authority will provide, upon request and when available, annual audited financial statements and other pertinent credit information relevant to the Authority's outstanding securities, including the Authority's Comprehensive Annual Financial Report, if one is prepared, and will provide copies to one or more major information providers in the state and local government securities market. In addition, appropriate periodic credit information necessary for maintaining the ratings on the Bonds will be provided by the Authority to the rating agencies rating the Bonds.

This Official Statement will be filed with one or more nationally recognized municipal securities information repositories.

PUERTO RICO PUBLIC BUILDINGS AUTHORITY

By: ....../s/ RAIMUNDO MATOS-IGLESIAS......
*Executive Director*

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# COMMONWEALTH OF PUERTO RICO

## Geography and Population

Puerto Rico, the fourth largest of the Caribbean islands, is located approximately 1,600 miles southeast of New York, New York and 1,000 miles east-southeast of Miami, Florida. It is approximately 100 miles long and 35 miles wide.

According to the United States Census Bureau, the population of Puerto Rico was approximately 3,522,000 in 1990 compared to 3,196,520 in 1980. As of 1990, the population of San Juan, the island's capital and largest city, was approximately 437,000.

## Relationship with the United States

Puerto Rico was discovered by Columbus in 1493, and the island was conquered and settled by the Spaniards shortly thereafter. It remained a Spanish possession for four centuries. Although the culture of Puerto Rico is primarily Hispanic, a considerable intermingling of Hispanic and United States cultures has occurred.

Puerto Rico came under United States sovereignty by the Treaty of Paris, signed on December 10, 1898, terminating the Spanish-American War. Puerto Ricans have been citizens of the United States since 1917. In July 1950, after a lengthy period of evolution toward greater self-government for Puerto Rico, the Congress of the United States enacted Public Law 600, which is in the nature of a compact and which became effective upon its acceptance by the electorate of Puerto Rico. It provided that those sections of existing law which defined the political, economic and fiscal relationship between Puerto Rico and the United States should remain in full force. It also authorized Puerto Rico to draft and approve its own Constitution. The Constitution was drafted by a popularly elected constitutional convention, overwhelmingly approved in a special referendum and approved "as a compact" by the United States Congress and the President, becoming effective upon proclamation of the Governor of Puerto Rico on July 25, 1952. Puerto Rico's relationship to the United States under the compact is referred to herein as commonwealth status.

The United States and the Commonwealth share a common defense, market and currency. The official languages of Puerto Rico are Spanish and English. The Commonwealth exercises virtually the same control over its internal affairs as do the fifty states; however, it differs from the states in its relationship with the federal government. The people of Puerto Rico are citizens of the United States but do not vote in national elections, and they are represented in Congress by a Resident Commissioner who has a voice in the House of Representatives but no vote. Most federal taxes, except those such as social security taxes which are imposed by mutual consent, are not levied in Puerto Rico. No federal income tax is collected from Commonwealth residents on ordinary income earned from sources in Puerto Rico, except for federal employees who are subject to taxes on their salaries. Federal excise taxes on shipments of alcoholic beverages of $10.50 per gallon and tobacco products from Puerto Rico to the mainland are returned to the Commonwealth Treasury.

## Governmental Structure

The Commonwealth's Constitution provides for the separation of powers of the executive, legislative and judicial branches of government. The Governor is elected every four years. The bicameral Legislature consists of a Senate and a House of Representatives and is elected for four-year terms. The highest court within the local judicial branch is the Supreme Court of Puerto Rico. Decisions of the Supreme Court of Puerto Rico may be appealed to the Supreme Court of the United States in the same manner and under the same terms and conditions that decisions may be appealed from state courts. Puerto Rico has a District Court of the United States for the District of Puerto Rico. Decisions of this court may be appealed to the United States Court of Appeals for the First Circuit and to the Supreme Court of the United States.

Governmental responsibilities assumed by the Commonwealth are similar in nature to those of the various state governments but more extensive in scope. The Commonwealth assumes responsibility for local police and fire protection, education, public health and welfare programs and economic development.

Pedro J. Rosselló was sworn in as Governor of Puerto Rico on January 2, 1993. He obtained a medical degree from Yale University in 1970, after completing his undergraduate studies at Notre Dame University in 1966, and specialized in General and Pediatric Surgery at Harvard University. In 1985 he was appointed Director of San Juan's Health Department, a position which he held for three years. As a member of the New Progressive Party, he was the party's candidate for Resident Commissioner to the U.S. Congress in 1988. In 1991 he was elected President of the New Progressive Party.

Manuel Díaz Saldaña, Secretary of the Treasury, took office in January 1993. He is a certified public accountant and a graduate of the University of Puerto Rico where he obtained a bachelor's degree in Business Administration and Accounting. Prior to his appointment, he worked for nineteen years as an accountant and auditor for various accounting firms.

Marcos Rodríguez-Ema, President of Government Development Bank, took office in January 1993. He obtained a Bachelor of Science degree (Cum Laude) in foreign service and a law degree from Georgetown University. Prior to his appointment, he worked for five years as a lawyer in a San Juan law firm and for six years as an investment banker for two major securities firms.

**Political Trends**

For many years there have been two major views in Puerto Rico with respect to the island's relationship to the United States, one favoring statehood, represented by the New Progressive Party, and the other essentially favoring the existing commonwealth status, represented by the Popular Democratic Party. The following table shows the percentages of the total vote received by the gubernatorial candidates of the various parties in the last five elections by voter preference with respect to statehood, commonwealth status and independence. While the electoral choices of Puerto Rico's voters are not made solely on the basis of preferences regarding the island's relationship with the United States, candidates who support a permanent relationship between Puerto Rico and the United States have dominated elections for many years.

| | 1976 | 1980 | 1984 | 1988 | 1992 |
|---|---|---|---|---|---|
| New Progressive Party | 48.3% | 47.3% | 45.5% | 45.8% | 49.9% |
| Popular Democratic Party | 45.3 | 47.0 | 48.5 | 48.7 | 45.9 |
| Puerto Rico Independence Party | 6.4 | 5.4 | 3.9 | 5.4 | 4.2 |
| Others | — | 0.3 | 2.1 | 0.1 | — |

The 1992 election saw control of the executive and legislative branches pass to the New Progressive Party. The composition of the Senate and House by the several political parties is as follows:

| | Senate | House |
|---|---|---|
| New Progressive Party | 30 | 36 |
| Popular Democratic Party | 8 | 16 |
| Puerto Rico Independence Party | 1 | 1 |
| | 39 | 53 |

The next general election (gubernatorial and legislative) in Puerto Rico will be held in November 1996. Voter participation in the Commonwealth has been substantially higher than in the rest of the United States, averaging 85% since 1972.

## THE ECONOMY

### General

The Commonwealth has established policies and programs directed at the development of manufacturing and the expansion and modernization of the island's infrastructure. The investment of mainland United States, foreign and local funds in new factories has been stimulated by selective tax exemption, development loans, and other financial and tax incentives. Infrastructure expansion and modernization have been to a large extent financed by bonds and notes issued by the Commonwealth, its public corporations and municipalities. Economic progress has been aided by significant increases in the levels of education and occupational skills of the island's population.

The economy of Puerto Rico is closely integrated with that of the mainland United States. During fiscal 1992 approximately 88% of Puerto Rico's exports were to the United States mainland, which was also the source of approximately 68% of Puerto Rico's imports. In fiscal 1992, Puerto Rico experienced a $2,940.3 million positive adjusted merchandise trade balance.

The economy of Puerto Rico is dominated by the manufacturing and service sectors. The manufacturing sector has experienced a basic change over the years as a result of increased emphasis on higher wage, high technology industries such as pharmaceuticals, electronics, computers, microprocessors, professional and scientific instruments, and certain high technology machinery and equipment. The service sector, including finance, insurance and real estate, also plays a major role in the economy. It ranks second only to manufacturing in contribution to the gross domestic product and leads all sectors in providing employment. In recent years, the service sector has experienced significant growth in response to the expansion of the manufacturing sector.

Gross product in fiscal 1988 was $18.6 billion, and gross product in fiscal 1992 was $23.6 billion ($19.5 billion in 1987 prices). This represents an increase in gross product of 27.3% from fiscal 1988 to 1992 (8.7% in 1987 prices).

Since fiscal 1987, personal income, both aggregate and per capita, has increased consistently each fiscal year. In fiscal 1992, aggregate personal income was $22.7 billion ($19.8 billion in 1987 prices) and personal income per capita was $6,360 ($5,546 in 1987 prices).

Personal income includes transfer payments to individuals in Puerto Rico under various social programs. Total federal payments to Puerto Rico, which include many types in addition to federal transfer payments, are lower on a per capita basis in Puerto Rico than in any state. Transfer payments to individuals in fiscal 1992 were $4.9 billion, of which $3.3 billion, or 67.3%, represent entitlements to individuals who had previously performed services or made contributions under programs such as Social Security, Veterans' Benefits and Medicare.

A discussion of highlights of the economy for the periods covering fiscal 1988 through fiscal 1992, and fiscal 1993 follows.

*Fiscal 1988 to 1992*

Puerto Rico's decade-long economic expansion continued throughout the five-year period from fiscal 1988 through fiscal 1992. Almost every sector of the economy was affected and record levels of employment were achieved. While trends in the Puerto Rico economy normally follow those in the United States, Puerto Rico did not experience a recession as did the United States primarily because of its strong manufacturing base which has a large component of non-cyclical industries. Other factors behind the expansion included Commonwealth-sponsored economic development programs, the relatively stable prices of oil imports, periodic declines in the exchange value of the United States dollar and the relatively low cost of borrowing during the period.

Average employment increased from 909,000 in fiscal 1988 to 977,000 in fiscal 1991. Average unemployment declined from 15.9% in fiscal 1988 to 15.2% in fiscal 1991. In fiscal 1992, average employment remained at the level of 1991, and unemployment increased to 16.5%.

The following table shows the gross product for the five fiscal years ended June 30, 1992.

**Commonwealth of Puerto Rico**

**Gross Product**

| | Fiscal Year Ended June 30 | | | | |
|---|---|---|---|---|---|
| | **1988** | **1989** | **1990** | **1991** | **1992(p)** |
| Gross product — $ millions | $18,550 | $19,954 | $21,619 | $22,857 | $23,620 |
| Real gross product — $ millions (1987 prices) | 17,915 | 18,620 | 19,093 | 19,240 | 19,474 |
| Annual percentage increase in real gross product (1987 prices) | 4.4% | 3.9% | 2.5% | 0.8% | 1.2% |
| U.S. annual percentage increase in real gross product (1987 prices) (1) | 4.1% | 3.4% | 1.8% | (0.7%) | 0.4% |

(p) Preliminary

(1) Restated to correspond to the Commonwealth's fiscal year ending June 30.
*Sources:* Planning Board and Data Resources Inc.

*Fiscal 1992*

In fiscal 1992, the Planning Board's Economic Activity Index, a composite index of thirteen economic indicators, increased 0.4% compared to fiscal 1991. The thirteen economic indicators are: total employment, manufacturing employment, manufacturing payroll, electric energy consumption, external trade, tourist hotel registrations, retail sales, excise taxes, electric energy production, new housing unit permits, hours worked, cement production, and new motor vehicle registrations. The Index may not necessarily change at the same percentage rate as the gross product of Puerto Rico.

Total employment in fiscal 1991 when compared to fiscal 1990 had increased by 1.5%. Total salaried employment as reflected in the Establishment Survey conducted by the Puerto Rico Department of Labor and Human Resources showed an annual increase of 0.6% in fiscal 1992. However, total employment as reflected in the Household Survey (includes agricultural and self employment), also conducted by the Department of Labor and Human Resources, averaged 977,000 in fiscal 1992, the same as 1991.

Economic growth continued in fiscal 1992, with a gross product increase of 1.2%.

*Fiscal 1993*

The Planning Board's Economic Activity Index increased 1.3% in the first eight months of fiscal 1993 compared to the same period of fiscal 1992, which period showed an increase of less than 0.1% over the same period of fiscal 1991.

In the first nine months of fiscal 1993, total employment (not seasonally adjusted) increased 2.1% when compared to the same period in fiscal 1992. Total employment averaged 994,000 in the first nine months of fiscal 1993 compared to 973,000 in the same period of fiscal 1992.

The Planning Board's most recent Gross Product forecast for fiscal 1993, made in February 1993, shows an increase of 2.9% over fiscal 1992. Actual growth in the Puerto Rico economy in fiscal 1993 will depend on several factors, including the state of the United States economy and the relative stability in the price of oil imports, the exchange value of the U.S. dollar and the cost of borrowing.

The present administration, which took office in January of this year, envisions major economic reforms and has developed a new economic development program to be implemented during the next few years. This program is structured on the premise that the private sector will be the primary vehicle for economic development and growth. It promotes changing the role of the government from one of being a provider of most basic services to serving as a facilitator for private sector initiatives and will encourage private sector investment by reducing regulatory restraints imposed by government.

The program contemplates the development of initiatives that will foster private investment, both external and internal, in areas that are served more efficiently and effectively by the private sector. The program also contemplates a general revision of the tax system to expand the tax base, reduce top personal and corporate tax rates and simplify a highly complex system.

Another important goal for the new program is to reduce the size of the government's direct contribution to gross domestic product. This would be realized through a reduction in government consumption and an increase in government investment in order to improve and expand Puerto Rico's infrastructure to facilitate private sector development and growth.

The new economic plan will identify and promote those economic sectors in which Puerto Rico can compete more effectively in the global markets. Tourism has been targeted as a top priority because of its potential for job creation and for an increased contribution to the gross domestic product stemming from Puerto Rico's natural competitive advantages.

**Employment and Unemployment**

The number of persons employed in Puerto Rico during fiscal 1992, averaged 977,000. Unemployment, although at a low level compared to the late seventies, remains above the average for the United States. The following table presents annual statistics of employment and unemployment from fiscal 1988 through fiscal 1992 and monthly statistics for July 1992 through March 1993.

**Commonwealth of Puerto Rico**

**Employment and Unemployment(1)**

| Fiscal Year Ended June 30 | Labor Force | Employed | Unemployed | Unemployment Rate(2) |
|---|---|---|---|---|
| | | (Annual Average) | | |
| 1988 | 1,081 | 908 | 172 | 15.9% |
| 1989 | 1,108 | 948 | 160 | 14.4 |
| 1990 | 1,124 | 963 | 160 | 14.3 |
| 1991 | 1,152 | 977 | 175 | 15.2 |
| 1992 | 1,170 | 977 | 193 | 16.5 |
| **Fiscal 1993** | | (Not Seasonally Adjusted) | | |
| July | 1,206 | 994 | 212 | 17.6 |
| August | 1,186 | 988 | 198 | 16.7 |
| September | 1,196 | 990 | 206 | 17.2 |
| October | 1,210 | 1,018 | 192 | 15.9 |
| November | 1,198 | 1,011 | 187 | 15.6 |
| December | 1,179 | 1,002 | 177 | 15.0 |
| January | 1,174 | 971 | 203 | 17.3 |
| February | 1,184 | 970 | 214 | 18.1 |
| March | 1,211 | 1,002 | 209 | 17.3 |

(1) Thousands of persons 16 years of age and over
(2) Unemployed as percentage of labor force
*Source:* Department of Labor and Human Resources — Household Survey

The United States minimum wage laws are generally applicable in Puerto Rico.

## Economic Performance by Sector

Puerto Rico has a diversified economy. During the fiscal years 1988-1992, the manufacturing and service sectors generated the largest portion of gross product. Three sectors of the economy provide the most employment: manufacturing, services and government.

The following table presents annual statistics of gross domestic product by sector and gross product for the five fiscal years ended June 30, 1992.

### Commonwealth of Puerto Rico

### Gross Domestic Product by Sector and Gross Product

| | Fiscal Year Ended June 30 | | | | |
|---|---|---|---|---|---|
| | 1988 | 1989 | 1990 | 1991 | 1992(p) |
| | (in millions at current prices) | | | | |
| Manufacturing | $10,513 | $11,133 | $12,126 | $12,762 | $13,155 |
| Services(1) | 9,920 | 10,537 | 11,318 | 11,969 | 12,671 |
| Government(2) | 2,918 | 3,187 | 3,337 | 3,538 | 3,738 |
| Transportation, communications and public utilities | 2,262 | 2,315 | 2,468 | 2,677 | 2,841 |
| Agriculture, forestry and fisheries | 399 | 443 | 434 | 449 | 462 |
| Construction(3) | 551 | 662 | 720 | 771 | 789 |
| Hotels | 255 | 289 | 321 | 331 | 342 |
| Statistical discrepancy | (640) | (298) | (121) | 94 | (28) |
| Total gross domestic product | 26,178 | 28,267 | 30,604 | 32,591 | 33,969 |
| Less: net payments abroad | 7,629 | 8,313 | 8,985 | 9,734 | 10,350 |
| Total gross product(4) | $18,550 | $19,954 | $21,619 | $22,857 | $23,620 |

(p) Preliminary
(1) Includes wholesale and retail trade; finance, insurance and real estate; and other services; excludes services in hotels
(2) Includes the Commonwealth, its municipalities and the federal government; excludes the public corporations
(3) Includes mining
(4) Totals may not add up due to rounding.

*Source:* Planning Board

The following table presents annual statistics of average employment by sector for the five fiscal years ended June 30, 1992.

### Commonwealth of Puerto Rico

### Average Employment by Sector

| | Fiscal Year Ended June 30 | | | | |
|---|---|---|---|---|---|
| | 1988 | 1989 | 1990 | 1991 | 1992(p) |
| | (thousands of persons age 16 and over) | | | | |
| Manufacturing | 163 | 165 | 168 | 164 | 164 |
| Services(1) | 400 | 419 | 421 | 448 | 449 |
| Government(2) | 209 | 219 | 222 | 217 | 219 |
| Transportation, communication and public utilities | 52 | 53 | 60 | 58 | 54 |
| Construction(3) | 52 | 55 | 56 | 55 | 56 |
| Agriculture, forestry and fisheries | 33 | 37 | 36 | 35 | 34 |
| Total(4) | 909 | 948 | 963 | 977 | 977 |

(p) Preliminary
(1) Includes wholesale and retail trade; finance, insurance and real estate; and other services
(2) Includes the Commonwealth, its municipalities and federal government; excludes the public corporations
(3) Includes mining
(4) Totals may not add up due to rounding

*Source:* Department of Labor and Human Resources — Household Survey

*Manufacturing*

Manufacturing is the largest sector in the economy of Puerto Rico in terms of gross domestic product. In fiscal 1992, the Planning Board estimates that manufacturing generated $13.2 billion, or 38.7% of gross domestic product. The manufacturing sector employed 151,460 workers of total employment in fiscal years 1991 and 1992 (as reported in the Department of Labor and Human Resources — Census of Manufacturing). Most of the island's manufacturing output is shipped to the mainland United States, which is also the principal source of semifinished manufactured articles on which further manufacturing operations are performed in Puerto Rico. As of December 1992, the average hourly manufacturing wage rate in Puerto Rico was approximately 57% of the average mainland United States rate.

Manufacturing in Puerto Rico is now more diversified than during the earlier phases of the industrial development program. In the last two decades, industrial development has tended to be more capital intensive and more dependent on skilled labor. This gradual shift in emphasis is perhaps best exemplified by the heavy investment in the pharmaceuticals, scientific instruments, computers, microprocessors, medical products, and electrical products industries over the last decade. The following table sets forth gross domestic product by manufacturing industry for the five fiscal years ended June 30, 1992.

**Commonwealth of Puerto Rico**

**Gross Domestic Product by Manufacturing Industry**

| | Fiscal Year Ended June 30 | | | | |
|---|---|---|---|---|---|
| | 1988 | 1989 | 1990 | 1991 | 1992 (p) |
| | (in millions at current prices) | | | | |
| Pharmaceuticals | $ 4,249 | $ 4,381 | $ 4,990 | $ 5,978 | $ 6,327 |
| Machinery and metal products | 2,881 | 2,992 | 3,205 | 2,914 | 2,772 |
| Food products | 1,374 | 1,540 | 1,791 | 1,846 | 1,941 |
| Apparel | 497 | 490 | 486 | 490 | 528 |
| Other(1) | 1,513 | 1,730 | 1,655 | 1,533 | 1,588 |
| Total gross domestic product by manufacturing industry | $10,513 | $11,133 | $12,126 | $12,761 | $13,155 |

(p) Preliminary

(1) Includes petroleum products; petrochemicals and other chemical products; tobacco products; stone, clay, and glass products; textiles; and others

*Source:* Planning Board

The following table sets forth manufacturing employment by industry group.

**Commonwealth of Puerto Rico**

**Manufacturing Employment by Industry Group**

| Industry Group | As of March 31 1988 | 1989 | 1990 | 1991 | 1992(p) |
|---|---|---|---|---|---|
| Apparel and related products | 33,624 | 32,187 | 31,238 | 29,841 | 30,875 |
| Food and related products | 23,625 | 24,173 | 23,385 | 20,059 | 20,928 |
| Electrical machinery, equipment and supplies | 22,796 | 20,863 | 20,567 | 19,361 | 17,923 |
| Chemicals and related products | 19,051 | 20,554 | 22,659 | 23,130 | 24,015 |
| Professional and scientific instruments | 13,785 | 14,861 | 14,798 | 16,341 | 15,838 |
| Machinery, except electrical and transportation equipment | 4,670 | 5,887 | 5,347 | 4,562 | 4,452 |
| Petroleum refining and related industries; rubber and miscellaneous plastic products | 7,207 | 7,417 | 6,708 | 6,296 | 5,763 |
| Leather and leather products | 5,931 | 5,640 | 6,284 | 5,904 | 6,057 |
| Paper and related products; printing, publishing and related industries | 5,431 | 5,637 | 5,768 | 6,056 | 5,991 |
| Metal products | 4,888 | 5,209 | 5,187 | 5,078 | 4,768 |
| Stone, clay and glass products | 4,621 | 4,950 | 5,136 | 4,808 | 4,755 |
| Lumber and wood products; furniture and fixtures | 3,505 | 3,207 | 3,425 | 2,787 | 2,953 |
| Textile mill products | 3,632 | 3,839 | 3,679 | 3,596 | 3,860 |
| Tobacco products | 1,162 | 1,177 | 1,089 | 917 | 935 |
| Miscellaneous manufacturing industries | 3,094 | 3,273 | 3,214 | 2,698 | 2,347 |
| Total | 157,022 | 158,874 | 158,484 | 151,434 | 151,460 |

(p) Preliminary

*Sources:* Department of Labor and Human Resources — Census of Manufacturing

## Leading United States and Foreign Companies With Manufacturing Operations In Puerto Rico

| Company | Product |
|---|---|
| **Employment 2,500 and over** | |
| Abbott Laboratories, Inc. | Pharmaceuticals |
| Baxter International | Pharmaceuticals |
| General Electric Co. | Electrical |
| H. J. Heinz Co. | Food |
| Johnson and Johnson | Pharmaceuticals |
| Sara Lee Corp. | Apparel |
| Westinghouse Electric Co. | Electrical |
| **Employment 1,500 to 2,499** | |
| Bristol-Myers-Squibb | Pharmaceuticals |
| Motorola Inc. | Electronic Components |
| P.L. Industries | Apparel |
| Propper International | Apparel |
| U.S. Surgical | Scientific Instruments |
| Warner-Lambert Co. | Pharmaceuticals |
| **Employment 1,000 to 1,499** | |
| American Cyanamid Co. | Pharmaceuticals and Medical Instruments |
| American Home Products | Pharmaceuticals |
| Avon Products Inc. | Costume Jewelry |
| Dexter Shoe | Footwear |
| DuPont E.I. de Nemours | Chemicals |
| Eli Lilly and Co. | Pharmaceuticals |
| Kendall Healthcare Co. | Medical Instruments |
| NCC Industries | Apparel |
| Schering-Plough Corp. | Pharmaceuticals |
| Timberland Company (The) | Leather |
| Uni Group | Food |
| **Employment 500 to 999** | |
| ARA Holding Group | Apparel |
| Becton-Dickinson & Co. | Scientific Instruments |
| Conagra | Food |
| Consolidated Cigar Ltd. | Tobacco and Leather |
| Dero Industries | Canvas |
| Dooney & Bourke | Leather |
| G.T.E. Products | Electrical Instruments |
| Hampshire Designers Knitting Mills | Textiles |
| Hoffman - La Roche | Pharmaceuticals |
| Hubbell Incorporated | Electrical Instruments |
| Insilco Corporation | Office Equipment |
| Intel | Computers |
| Kicks Fashions | Apparel |
| Maidenform | Apparel |
| Medtronics | Surgical and Medical Instruments |
| Merck & Co. | Chemicals |
| Monsanto | Pharmaceuticals |
| Morse Shoe | Footwear |
| Owens Illinois | Glass and Plastics |
| Pall Corp. | Filters |
| Pfizer | Pharmaceuticals |
| Phillips Van-Heusen | Apparel and Footwear |
| RJR Nabisco | Food and Cigarettes |
| Sea Board Corp. | Food |
| Sensormatic Electronics | Electronic |
| Smith-Kline Beeckman | Pharmaceuticals |
| Storage Technology | Electronic |
| Up-John Co. | Pharmaceuticals |
| Warnaco | Apparel |
| Wickes Companies | Apparel |
| Williamson-Dickie Mfg. | Apparel |
| Wolverine World Wide | Footwear |
| **Employment 300 to 499** | |
| ABB Asea Brown Bovery Ltd. | Precision Instruments |
| Allergan | Pharmaceuticals |
| Amity Leather Products | Leather |
| Borden Inc. | Food |
| Coca-Cola | Food |
| Check-point Systems Inc. | Electronic |
| DSC Communication Corp. | Electronic |
| Eagle Work Clothes | Apparel |
| Eastman Kodak Co. | Electronic |
| Echlin Mfg. | Motor Vehicles Parts |
| Emerson Electric | Electronic and Scientific Instruments |
| Filtertek Inc. | Filters |
| Formflex Foundations | Apparel |
| Garment Corporation of America | Apparel |
| Granada Sales | Apparel |
| General Instruments Co. | Communications |
| Harvard Industries | Glass |
| Hewlett-Packard | Computers |
| Inner World | Apparel |
| Isla Verde Investment | Apparel |
| Isratex Inc. | Apparel |
| Les Ciments Français | Cement |
| Matsushita Electric | Electrical |
| Maurice Silvera Inc. | Apparel |
| Millipore | Scientific Instruments |
| Minnetonka Moccasin | Footwear |
| Mitsubishi Corp. | Food |
| Nantucket Mills | Apparel |
| Nestle S.A. | Pharmaceuticals |
| Nypro | Plastics |
| Penn-State Coats & Aprons | Apparel |
| Procter & Gamble Co. | Pharmaceuticals |
| Power One | Electrical |
| R.E. Phelon & Co. | Electronics |
| Randa Corporation | Textiles |
| Rexene Corp. | Corrugated Boxes |
| Rexon Inc. | Electronics |
| Standard Motor Products | Motor Vehicles Parts |
| Sun Co. | Oil Refining |
| Syntex | Pharmaceuticals |
| Unilever | Consumers & Medicals |
| Wheaton Industries | Plastics Products |

*Source:* Economic Development Administration, Office of Economic Research (as of March 1993)

*Services*

Puerto Rico has experienced significant growth in the services sector in terms of both income and employment over the past decade, showing a favorable trend as compared with certain other industrialized economies. During the period between 1971 and 1992, the gross domestic product in the services sector increased at an annual average rate of 9.3%. Employment in this sector increased at an annual average rate of 3.1%. The development of the services sector in the local economy has shown a strong interaction among the following important sectors: manufacturing, tourism, construction and agriculture. The services sector in Puerto Rico has a diversified base.

The high degree of knowledge, skills, and expertise in professional and technical services available in Puerto Rico places Puerto Rico in a competitive position with respect to Latin America and other trading countries throughout the world. A major element in the economic program of the present administration is the further development of the local services sector which has the capacity to increase its export potential and to generate more income and jobs during the coming years.

The service sector ranks second to manufacturing in its contribution to gross domestic product, and it is the sector with the greatest employment. In fiscal 1992, services generated $13.0 billion of gross domestic product, or 38.3% of the total. Service employment in fiscal 1992 was 449,000 workers, or 46.0% of total employment. Wholesale and retail trade and finance, insurance and real estate have experienced significant growth in the fiscal 1988 to 1992 period, as measured by gross domestic product. Gross domestic product in the wholesale and retail trade increased from $4.1 billion in fiscal 1988 to $5.0 billion in fiscal 1992. In finance, insurance and real estate, gross domestic product increased from $3.5 billion in fiscal 1988 to $4.5 billion in fiscal 1992. There are twenty commercial banks and trust companies currently operating in Puerto Rico of which three are U.S. major money center banks, three are other foreign banks and fourteen are local banks and trust companies. Total assets of these institutions as of June 30, 1992 were $23.1 billion. In addition, eight federal thrift institutions operate on the island with estimated total assets of $4.2 billion as of June 30, 1992 and eight major investment banks maintain operations in Puerto Rico. The following tables set forth gross domestic product and service sector employment for the five fiscal years ended June 30, 1992.

**Commonwealth of Puerto Rico**

**Gross Domestic Product by Service Industry**

| | Fiscal Year Ended June 30 | | | | |
|---|---|---|---|---|---|
| | 1988 | 1989 | 1990 | 1991 | 1992(p) |
| | (in millions, at current prices) | | | | |
| Wholesale and retail trade | $ 4,376 | $ 4,376 | $ 4,728 | $ 4,811 | $ 5,008 |
| Finance, insurance and real estate | 3,750 | 3,750 | 3,896 | 4,205 | 4,458 |
| Hotels | 289 | 289 | 321 | 331 | 342 |
| Other services | 2,249 | 2,411 | 2,694 | 2,953 | 3,205 |
| Total(1) | $10,175 | $10,826 | $11,639 | $12,300 | $13,013 |

(p) Preliminary

(1) Totals may not add up due to rounding.

*Source:* Planning Board

**Commonwealth of Puerto Rico**

**Average Employment by Service Sector**

| | Fiscal Year Ended June 30 | | | | |
|---|---|---|---|---|---|
| | 1988 | 1989 | 1990 | 1991 | 1992(p) |
| | (thousands of persons aged 16 and over) | | | | |
| Wholesale and retail trade | 180 | 186 | 185 | 195 | 193 |
| Finance, insurance and real estate | 31 | 32 | 32 | 32 | 32 |
| Other services(1) | 189 | 201 | 206 | 221 | 224 |
| Total(2) | 400 | 419 | 421 | 448 | 449 |

(p) Preliminary

(1) Including Tourism

(2) Totals may not add up due to rounding.

*Source:* Department of Labor and Human Resources — Household Survey

*Government*

The government sector of the Commonwealth plays an important role in the economy of the island. In fiscal 1992, the government accounted for $3.7 billion of Puerto Rico's gross domestic product, or 11.0% of the total. The government is also a significant employer, providing jobs for 219,000 workers, or 22.4% of total employment in fiscal 1992. The government sector employment does not include data relating to certain public corporations which are included in other sectors. These public corporations include such significant employers as the Electric Power Authority, the Telephone Authority and the Aqueduct and Sewer Authority, among others.

*Tourism*

Tourism expenditures were 6.4% of the island's gross product in fiscal 1992. Tourist expenditures and the number of visitors have grown consistently since 1985, reaching $1.5 billion and more than 3.7 million respectively, in fiscal 1992. Since fiscal 1987, a number of major hotels have undergone substantial renovation. Several international hotel corporations have recently made or are expected to make substantial capital investments to develop additional tourist facilities. Further private development of new hotel facilities and tourist attraction areas in Puerto Rico is being considered. The average number of hotel rooms available for fiscal 1992 was 6,281.

Several cruise ships use San Juan as their home port. San Juan is the second largest cruise ship port in the world. Total cruise ship visitors in fiscal 1992 exceeded 1.0 million for the first time, a 2.3% increase over fiscal 1991. The following table presents data relating to visitors to Puerto Rico and tourist expenditures for the five fiscal years ended June 30, 1992.

**Commonwealth of Puerto Rico**

**Tourism Data**

| Fiscal Year Ended June 30 | Number of Visitors | | | | |
|---|---|---|---|---|---|
| | Tourist Hotel(1) | Cruise Ship | Other(1) | Total | Tourist Expenditures (in millions) |
| 1988 | 616,510 | 723,724 | 1,664,002 | 3,004,236 | $1,121.4 |
| 1989 | 651,842 | 777,405 | 1,791,943 | 3,221,190 | 1,254.0 |
| 1990 | 659,013 | 866,090 | 1,900,734 | 3,425,827 | 1,366.4 |
| 1991 | 650,115 | 891,348 | 1,962,876 | 3,504,339 | 1,435.7 |
| 1992(p) | 653,545 | 1,063,370 | 1,986,266 | 3,703,181 | 1,511.3 |

(p) Preliminary

(1) Including visitors in homes of relatives, friends and in hotel apartments

*Source:* Puerto Rico Tourism Company and the Planning Board

During the first eight months of fiscal 1993, the number of persons registered in tourist hotels totalled 599,700, an 8.9% increase over the same period in fiscal 1992. The average of the occupancy rate in tourist hotels increased 1.9% in the first eight months of fiscal 1993 as compared with the same period in fiscal 1992.

*Transportation*

Thirty-four shipping lines offer regular ocean freight service to eighty United States and foreign ports. San Juan is the island's leading seaport, but there are also seaport facilities at other locations on the island.

The San Juan Luis Muñoz Marín International Airport is currently served by 28 United States and international airlines. At present, there is daily direct service between San Juan and New York, Chicago, Dallas, Los Angeles, Miami, Atlanta, Boston and numerous other United States cities. There is also regularly scheduled service between Puerto Rico and other Caribbean islands and major Latin American and European cities. A major United States airline uses San Juan as a hub for its intra-Caribbean service. Several smaller airports serve intra-island traffic.

The island's major cities are connected by a modern highway system which as of June 30, 1992, totaled approximately 9,100 miles.

*Agriculture*

The Commonwealth has traditionally supported the agricultural sector. In 1985, the Department of Agriculture initiated a program to promote and develop agricultural potential. The efforts of the Department of Agriculture and related agencies are being directed to increase and improve local agricultural production, increase efficiency and quality of produce and stimulate import substitution where economically feasible. In the last few years, non-traditional crops and livestock products have contributed a higher percentage of the sector's income.

The Commonwealth supports agricultural activities through incentives, subsidies and technical and support services, in addition to income tax exemptions for qualified income derived by bona fide farmers. Act No. 106, approved July 10, 1986, extended the exemption period from 10 to 15 years. The exemption from taxation during the entire 15-year period is set at 90%.

*Construction*

The construction industry has experienced substantial real growth since fiscal 1987. In fiscal 1992, the investment in construction rose to a record $2.7 billion as compared to $2.6 billion for fiscal 1991. The construction sector experienced a 12.0% decrease in total value of construction permits and a decrease of 1.3% in local cement consumption for fiscal 1992 when compared to fiscal 1991. During the first eight months of fiscal 1993, the total value of construction permits increased 20% and local cement consumption increased 0.5%, in comparison with the same period in fiscal 1992. Construction employment increased to 56,000 in fiscal 1992 from 55,000 in fiscal 1991.

**Higher Education**

During the past four decades, Puerto Rico has made significant advances in the field of education, particularly at the college and graduate school level. The transformation of Puerto Rico during the 1950's and 1960's from an agricultural economy to an industrial economy brought about an increased demand for education at all levels. Since 1970, the manufacturing sector has attracted more high technology industries in Puerto Rico. This has resulted in an increased demand for workers having a higher level of education in general and, in particular, greater expertise in various technical fields. During the same time period, enrollments in institutions of higher learning have risen very rapidly. This trend is due not only to growth in the college-age population, but also to the increasing proportion of college attendance by the college-age population.

The University of Puerto Rico, the only public university in Puerto Rico, includes eleven campuses located throughout the island. Total enrollment of the University was approximately 54,450 in 1992. The Commonwealth is legally obligated to annually appropriate to the University an amount equal to 9.0% (9.33% beginning July 1, 1993) of the average of the annual revenues from internal sources in each of the two fiscal years immediately preceding the current fiscal year.

The following table presents comparative trend data for Puerto Rico and the United States with respect to college age population and percentage of such population attending institutions of higher learning.

**Trend in College Enrollment**

| | Puerto Rico | | | Mainland United States | | |
|---|---|---|---|---|---|---|
| Academic Year | Population 18-24 Years of Age | Higher Education Enrollment | Percent(1) | Population 18-24 Years of Age | Higher Education Enrollment | Percent(1) |
| 1970 ........ | 341,448 | 57,338 | 16.8% | 23,989,000 | 8,580,887 | 35.8% |
| 1980 ........ | 397,839 | 130,105 | 32.7 | 30,093,000 | 12,096,895 | 40.2% |
| 1990 ........ | 397,600 | 156,147 | 39.3 | 26,140,000(2) | 13,213,000(2) | 50.5% |

(1) Number of persons of all ages enrolled in institutions of higher education as percent of population 18-24 years of age

(2) Estimated

*Sources:* Planning Board, U.S. Bureau of the Census, U.S. National Center for Education Statistics and Council on Higher Education of Puerto Rico

The table demonstrates that higher education enrollment in Puerto Rico has continued to increase despite slower growth in the college-age population.

In addition to the University of Puerto Rico, there are 5 other public and 33 private institutions of higher education located in Puerto Rico. Such institutions have current enrollments of approximately 103,100 students and provide programs of study in liberal arts, education, business, natural sciences, technology, secretarial and computer sciences, nursing, medicine and law. Degrees are offered by these institutions at the associate, bachelor's, master's and doctoral levels.

**Tax Incentives**

Much of the development of the manufacturing sector in Puerto Rico can be attributed to various federal and Commonwealth tax incentives, most notably Section 936 of the Internal Revenue Code of 1986, as amended (the "Code"), and the Commonwealth's Industrial Incentives Program.

*Section 936*

Under Section 936 of the Code, United States corporations that meet certain requirements and elect its application ("Section 936 Corporations") are entitled to credit against their United States corporate income tax the portion of such tax attributable to (i) income derived from the active conduct of a trade or business within Puerto Rico ("active business income") or from the sale or exchange of substantially all assets used in the active conduct of such trade or business and (ii) qualified possession source investment income ("passive income").

To qualify under Section 936 in any given taxable year a corporation must derive (i) for the three-year period immediately preceding the end of such taxable year 80% or more of its gross income from sources within Puerto Rico and (ii) for taxable years beginning after December 31, 1986, 75% or more of its gross income from the active conduct of a trade or business in Puerto Rico.

A Section 936 Corporation may elect to compute its active business income eligible for the Section 936 credit under one of three formulas: (A) a cost sharing formula, whereby it is allowed to claim all profits attributable to manufacturing intangibles and other functions carried out in Puerto Rico, provided it contributes to the research and development expenses of its affiliated group or pays certain royalties; (B) a profit split formula, whereby it is allowed to claim 50% of the net income of its affiliated group from the sale of products manufactured in Puerto Rico; or (C) a cost plus formula, whereby it is allowed to claim a reasonable profit on the manufacturing costs incurred in Puerto Rico. To be eligible for the first two formulas, the Section 936 Corporation must have a significant business presence for purposes of the Section 936 rules. *See*

"Recent Federal Legislative Proposals — Internal Revenue Code Section 936" under *The Economy* for a description of federal legislation and Clinton administration proposals affecting Section 936.

*Industrial Incentives Program*

Since 1948 Puerto Rico has had various industrial incentives laws designed to stimulate industrial investment in the island. Under these laws, companies engaged in manufacturing and certain other designated activities (such as hotel operations) were eligible to receive full or partial exemption from income, property and certain local taxes.

On January 24, 1987, the Governor of Puerto Rico signed into law the most recent industrial incentives law, Act No. 8 of January 24, 1987, known as the Puerto Rico Tax Incentives Act (the "1987 Act"). The tax exemption benefits provided by the 1987 Act are generally more favorable than those provided by its predecessor, the Industrial Incentives Act of 1978 (the "1978 Act"). The activities eligible for exemption under the 1987 Act include manufacturing, certain designated services for markets outside Puerto Rico, the production of energy from local renewable sources for consumption in Puerto Rico, and laboratories for scientific and industrial research.

The 1987 Act provides a fixed 90% exemption from income and property taxes and a 60% exemption from municipal license taxes during a 10, 15, 20 or 25 year period, depending on the zone where the operations are located. This initial exemption period may be extended for an additional 10 years at lower exemption rates. The 1987 Act also provides a special deduction equal to 15% of the production payroll for companies whose net income from operations is less than $20,000 per production job. This special benefit is designed to attract and maintain labor intensive operations in Puerto Rico. The passive income from certain qualified investments in Puerto Rico and the instruments evidencing such investments are fully exempt from tax. In addition, companies making such investments for fixed periods of not less than five years are eligible to reduce the tollgate tax imposed on dividend and liquidating distributions from a maximum rate of 10% to zero, depending on the amount and term of the investment.

The 1987 Act imposes a special surtax on sales volume designed to raise revenues to fund a special government program of scientific and technical research for the development of new products and industrial processes and the creation of special training programs for the chronically unemployed.

The 1987 Act applies to newly established operations as well as to existing operations that elect to convert their tax exemption grants to the provisions of the 1987 Act. Companies with existing operations that elect not to convert remain subject to the provisions of the 1978 Act or any of the predecessor industrial incentives laws.

Since 1983 hotel operations have been covered by a special incentives law, the Tourism Incentives Act of 1983, which provides exemptions from income, property and municipal license taxes for a period of 10 years. The income tax exemption rates vary depending on the zone where the business is located.

**Caribbean Basin Initiative**

In August, 1983, the President of the United States signed into law the Caribbean Basin Economic Recovery Act. The Tax Reform Act of 1986 amended Section 936 to allow Puerto Rico financial institutions, including Government Development Bank and Puerto Rico Economic Development Bank, to invest funds representing earnings accumulated under Section 936, in active business assets or development projects in a qualified Caribbean basin country. Such investments must be in accordance with a specific authorization from the Commissioner of Financial Institutions pursuant to regulations issued by the Secretary of the Treasury. As of December 1992, 117 projects under the Puerto Rico Caribbean Development Program have been promoted in thirteen Caribbean Basin countries, representing 29,801 jobs and over $1,183 million in loan commitments, of which $678 million of Section 936 funds have been disbursed.

The Caribbean Basin Projects Financing Authority ("CARIFA"), was created in 1989 with the power to issue revenue bonds, thus providing private entities with lower cost financing for eligible projects in the Caribbean region. As of April 30, 1993, CARIFA has financed eight projects in six Caribbean countries for a total investment of over $400 million.

**Recent Federal Legislative Proposals**

*Internal Revenue Code Section 936*

On February 16, 1993, legislation was introduced in the United States Senate to repeal Section 936 and replace it with a wage-based employment tax credit of 40% on qualified wages together with a disallowance of the deduction for such wages. Corporations which have elected Section 936 status would be entitled to a five-year transition period beginning with the taxable year which includes February 16, 1993. Under this proposed legislation, the permanent wage credit would equal 4% of qualified wages, up to a maximum amount of qualified wages per employee of $20,000, because of the disallowance of the deduction for such wages.

The following day, President Clinton proposed, as part of his economic plan, to replace the Section 936 income tax credit with a wage-based employment tax credit. The current version of the President's proposal seeks a 60% wage credit. In addition, under the President's proposal, the current tax-exemption on qualified possession source investment income (passive income) would be limited to income derived from 80% of a corporation's qualified tangible business investment in Puerto Rico. Corporations availing themselves of the Section 936 tax credit also would be able to deduct the amount of taxes paid in Puerto Rico from their federal income tax liability. The President's proposal would allow such corporations to continue to calculate tax benefits over a two-year phase-out period beginning after December 31, 1993 as they currently do, giving such corporations the option to claim 80% of their current Section 936 tax credit the first year and 60% the second year. The President's proposal limits the amount of qualified wages taken into account per employee to the maximum amount of eligible wages for social security tax purposes and does not disallow the deduction for such eligible wages. On May 13, 1993, the Committee on Ways and Means of the United States House of Representatives voted favorably on and sent to the full House for consideration certain elements of President Clinton's economic program, including the President's proposed revisions to Section 936 set forth above. The Committee added to the changes to Section 936 a requirement that any corporation electing the Section 936 credit and which relocates its operations to Puerto Rico must certify that such relocation will not adversely affect employment in the jurisdiction it is leaving. Such a requirement is similar to an existing requirement of the Department of the Treasury of Puerto Rico regarding such relocations.

The Government of Puerto Rico believes that the current proposal of the President would ask Puerto Rico to bear a disproportionate share of the burden in the President's deficit reduction plan. The Clinton administration has stated that it is continuing to review the President's proposal and is consulting with representatives of the Government of Puerto Rico.

On April 27, 1993, the Governor of Puerto Rico presented a counter-proposal on Section 936 in testimony before the Committee on Finance of the United States Senate. Under the Governor's proposal, Section 936 corporations may choose one of two options, either a compensation-based credit or an income-based incentive. Under the compensation-based option, Section 936 corporations may elect a credit against their federal income tax liability equal to 100% of (i) total compensation paid to their employees in Puerto Rico, including all fringe benefits and payroll taxes, plus (ii) all Puerto Rico income taxes and taxes on dividends paid by them (up to a maximum of 9%), plus (iii) all qualified possession source investment income (passive income). In addition, under this option, Section 936 corporations may receive an investment tax credit of 10% of new investment in plant, machinery and equipment. In the alternative, Section 936 corporations may select an income-based incentive of (i) 90% of the current Section 936 credit in 1994 and (ii) 80% of such credit in 1995 and in succeeding years. In addition, under this option, Section 936 corporations will continue to receive the full Section 936 credit for all qualified possession source investment income (passive income) as under current law.

It is not possible at this time to determine what legislative changes, if any, will be made to Section 936.

*NAFTA*

The United States, Canada and Mexico have entered into the North American Free Trade Agreement ("NAFTA"), an agreement in principle currently under consideration by the United States Senate, which agreement is designed to eliminate restrictions on trade and investment flows among the three countries. According to a study of the potential economic impact of NAFTA on the economy of Puerto Rico conducted by KPMG Peat Marwick for Government Development Bank, certain of the Commonwealth's industries, including those that are lower salaried and labor intensive, may face increased competition from Mexico, while

Puerto Rico's favorable investment environment, highly skilled work force, infrastructure development and tax structure (mainly Section 936) would tend to create expanded trade opportunities for Puerto Rico in such areas as pharmaceuticals and high technology manufacturing, were NAFTA to be ratified.

## DEBT

### Public Sector Debt

Public sector debt comprises bonds and notes of the Commonwealth and its municipalities and public corporations ("notes" as used in this Section is intended to refer to certain types of non-bond debt regardless of maturity), subject to the exclusions described in the following paragraph. Direct debt of the Commonwealth is supported by Commonwealth taxes. Debt of municipalities, other than bond anticipation notes, is supported by real and personal property taxes and municipal license taxes. Debt of public corporations, other than bond anticipation notes, is generally supported by the revenues of such corporations from charges for services or products. *See Public Corporations.* However, certain debt of public corporations is supported, in whole or in part, directly or indirectly, by Commonwealth appropriations or taxes.

The following table presents a summary of public sector debt as of February 28, 1993. Excluded from this table is debt not primarily payable from either Commonwealth or local taxes, or Commonwealth appropriations or public corporation charges for services or products. Also excluded from the following table is debt the inclusion of which would reflect double counting, including, but not limited to, $299,629,219 of bonds issued by Municipal Finance Agency to finance its purchase of bonds of Commonwealth municipalities; $2,228,345,000 of obligations of Government Development Bank issued to purchase certain Commonwealth public sector debt and for other purposes, of which $292,000,000 are guaranteed by the Commonwealth.

**Commonwealth of Puerto Rico**

**Public Sector Debt**

| | February 28, 1993 (in thousands) |
|---|---|
| Commonwealth direct debt | $ 4,003,394 |
| Municipal debt | 515,732 |
| Public corporation debt: | |
| Commonwealth guaranteed debt(1) | 151,695 |
| Debt supported by Commonwealth appropriations or taxes(2) | 3,927,839 |
| Non-guaranteed debt | 5,921,483 |
| Total public corporation debt(3) | 10,001,017 |
| Total public sector debt | $14,520,143 |

(1) Excludes $1,147,382,000 of Public Buildings Authority bonds and notes which are primarily payable from Commonwealth appropriations. All bonds and notes guaranteed by the Commonwealth are being paid by the public corporations which issued such bonds, see "Other Public Corporations" under *Public Corporations.*

(2) Represents bonds or notes, including bonds and notes issued by Aqueduct and Sewer Authority, Highway and Transportation Authority, Housing Bank and Finance Agency, Public Buildings Authority, Sugar Corporation, Infrastructure Financing Authority, Economic Development Bank, Health Facilities and Services Administration ("AFASS") and Agriculture and Commercial Development Corp. See "Other Public Corporations" under *Public Corporations.*

(3) Does not reflect the issuance on April 13, 1993 of $695,925,000 Puerto Rico Telephone Authority Revenue Refunding Bonds, Series M and of $48,550,000 Puerto Rico Telephone Authority Revenue Bonds, Series N (the "1993 Telephone Authority Bonds").

*Sources:* Government Development Bank and Department of the Treasury

No deductions have been made in the above table for debt service funds and debt service reserve funds. The table above and the amounts shown throughout this section as representing outstanding debt include outstanding capital appreciation bonds at their respective original principal amounts and do not include any accretion thereon.

## Debt Service Requirements for Commonwealth General Obligation Bonds

The following table presents debt service requirements for outstanding general obligation bonds. Debt service requirements for each fiscal year, as shown in the following table, include principal and interest due on July 1 of the next fiscal year.

**Commonwealth of Puerto Rico**

**Debt Service Requirements (in thousands)**

| Fiscal Year Ending June 30 | Outstanding Principal | Outstanding Interest | Total |
|---|---|---|---|
| 1993 | $ 156,475 | $ 206,678 | $ 363,153 |
| 1994 | 159,655 | 202,619 | 362,274 |
| 1995 | 173,820 | 194,072 | 367,892 |
| 1996 | 181,780 | 182,498 | 364,278 |
| 1997 | 186,045 | 172,886 | 358,931 |
| 1998 | 186,601 | 164,631 | 351,232 |
| 1999 | 175,661 | 158,176 | 333,837 |
| 2000 | 166,855 | 142,561 | 309,416 |
| 2001 | 167,991 | 132,050 | 300,041 |
| 2002 | 167,264 | 122,463 | 289,727 |
| 2003 | 96,454 | 191,004 | 287,458 |
| 2004 | 98,695 | 187,544 | 286,239 |
| 2005 | 172,682 | 109,991 | 282,673 |
| 2006 | 132,488 | 125,277 | 257,765 |
| 2007 | 104,624 | 132,348 | 236,972 |
| 2008 | 80,373 | 94,757 | 175,130 |
| 2009 | 82,885 | 74,128 | 157,013 |
| 2010 | 88,600 | 67,917 | 156,517 |
| 2011 | 92,787 | 63,242 | 156,029 |
| 2012 | 98,385 | 50,640 | 149,025 |
| 2013 | 85,930 | 45,427 | 131,357 |
| 2014 | 71,630 | 39,057 | 110,687 |
| 2015 | 76,130 | 34,547 | 110,677 |
| 2016 | 79,970 | 30,748 | 110,718 |
| 2017 | 85,790 | 25,001 | 110,791 |
| 2018 | 90,665 | 20,183 | 110,848 |
| 2019 | 75,825 | 14,039 | 89,864 |
| 2020 | 81,655 | 9,413 | 91,068 |
| 2021 | 43,715 | 4,125 | 47,840 |
| 2022 | 21,965 | 1,318 | 23,283 |
| | $3,483,395 | $2,999,340 | $6,482,735 |

*Source:* Government Development Bank and Department of the Treasury

### Commonwealth Guaranteed Debt

Annual debt service on outstanding Commonwealth guaranteed bonds issued by Urban Renewal and Housing Corporation and assumed in fiscal 1992 by Housing Bank and Finance Agency is $13,254,122 in the fiscal year ending September 30, 1993, which constitutes the maximum annual debt service on such bonds. The final maturity of such bonds is October 1, 2001. Annual debt service on Commonwealth guaranteed bonds of Public Buildings Authority is $102,591,681 in fiscal 1994 with the final maturity on July 1, 2021.

No payments under the Commonwealth guaranty have been required for bonds of Urban Renewal and Housing Corporation, Housing Bank and Finance Agency or Public Buildings Authority.

As of February 28, 1993, $292,000,000 of Commonwealth guaranteed obligations of Government Development Bank were outstanding. No payments under the Commonwealth guaranty have been required for any obligations of Government Development Bank.

The Farm Credit Corporation ("Farm Credit"), created pursuant to Act No. 68, approved June 8, 1960, as amended, assumed responsibility in 1971 for the administration of the Farm Credit Security Fund (the "Security Fund") from the Department of Agriculture. The Security Fund has guaranteed, under the good faith and credit of the Commonwealth, certain loans made by financial institutions and Farm Credit to farmers. The Security Fund is authorized to guarantee loans of which approximately $24,800,000 has been committed as of April 30, 1993. As of April 30, 1993, approximately $5,567,000 was available in the Security Fund to cover loan payment defaults by farmers. No payments under the Commonwealth guaranty have been required for any of the loans made by Farm Credit or private institutions which are guaranteed by the Security Fund. The Commercial and Agricultural Credit and Development Corporation has been created to provide, among other things, loans to the commercial and agricultural sectors. The functions of Farm Credit and the administration of the Security Fund have been transferred to the new public corporation, which is an affiliate of Economic Development Bank. Simultaneously with the creation of the new corporation, the amount of guarantees was limited to the outstanding loans which carry such guaranty. A joint resolution adopted by the Legislature on August 19, 1990 appropriates $8,000,000 per year beginning fiscal 1993 for five years to provide funds for the Security Fund. The proceeds of these appropriations will be used to pay a $40,000,000 loan made to the Fund by Government Development Bank which is being used to cover payment on loans guaranteed by the Fund.

### Trends of Public Sector Debt

Historically, the Commonwealth has maintained a fiscal policy which provides for a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. The Commonwealth also sought opportunities to realize debt service savings by refunding outstanding debt with obligations bearing lower interest rates. In certain years, this policy has had the effect of increasing the rate of growth of public sector debt above that of gross product. Over fiscal years 1988 to 1992, public sector debt increased 27.9% while gross product rose 27.3%. Short-term debt outstanding relative to total debt was 8.7% as of February 28, 1993.

Commonwealth debt management in recent years has also emphasized the control and reduction of short-term debt relative to total debt.

The following table shows the trends in gross product (in current dollars) and public sector debt for the five fiscal years ended June 30, 1992 and for the eight month period ended February 28, 1993.

**Commonwealth of Puerto Rico**

**Public Sector Debt and Gross Product**

| | Public Sector Debt | | | | | Gross Product(1) | |
|---|---|---|---|---|---|---|---|
| June 30 | Long Term | Short Term(2) | Short Term as % of Total | Total | Rate of Increase | Amount | Rate of Increase |
| | (dollars in millions) | | | | | | |
| 1988 | $10,149 | $ 658(3) | 6.1% | $10,807 | 6.6% | $18,550 | 8.1% |
| 1989 | 11,066 | 580(3) | 5.0 | 11,646 | 7.8 | 19,954 | 7.6 |
| 1990 | 11,492 | 1,073(3) | 8.5 | 12,565 | 7.9 | 21,619 | 8.3 |
| 1991 | 12,041 | 784(3) | 6.1 | 12,825 | 2.4 | 22,857 | 5.7 |
| 1992 | 13,108 | 713 | 5.2 | 13,821 | 8.1 | 23,620 | 3.3 |
| February 28, 1993 | 13,256 | 1,264 | 8.7 | 14,520 | 5.0 | N/A | N/A |

(1) In current dollars.
(2) Obligations with a maturity of three years or less are considered short-term debt.
(3) Does not include the tax and revenue anticipation notes which were outstanding at the close of the indicated fiscal years because sufficient funds had been set aside for the payment of such notes in full prior to the end of said fiscal years.

*Source:* Government Development Bank

The following table shows the trend of public sector debt by major category for the five fiscal years ended June 30, 1992 and the eight month period ended February 28, 1993.

**Commonwealth of Puerto Rico**

**Public Sector Debt by Major Category**

| | Commonwealth(1) | | | Municipalities | | | Public Corporations(2) | | | Total | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| June 30 | Long Term | Short Term(3) | Total | Long Term | Short Term(3) | Total | Long Term | Short Term(3) | Total | Long Term | Short Term(3) | Total |
| | (in millions) | | | | | | | | | | | |
| 1988 | $2,637 | —(4) | $2,637 | $366 | $30 | $396 | $7,146 | $628 | $ 7,774 | $10,149 | $ 658 | $10,807 |
| 1989 | 2,967 | —(4) | 2,967 | 375 | 24 | 399 | 7,724 | 555 | 8,279 | 11,066 | 580 | 11,646 |
| 1990 | 2,861 | 335(4) | 3,196 | 366 | 24 | 390 | 8,265 | 714 | 8,979 | 11,492 | 1,073 | 12,565 |
| 1991 | 3,260 | 54(4) | 3,314 | 386 | 30 | 416 | 8,395 | 700 | 9,095 | 12,041 | 784 | 12,825 |
| 1992 | 3,402 | — | 3,402 | 460 | 39 | 499 | 9,246 | 675 | 9,921 | 13,108 | 713 | 13,821 |
| February 28, 1993 | 3,603 | 400(5) | 4,003 | 484 | 32 | 516 | 9,169 | 832 | 10,001 | 13,256 | 1,264 | 14,520 |

(1) General obligation and other direct debt
(2) Includes Commonwealth guaranteed debt
(3) Obligations with a maturity of three years or less are considered short-term debt.
(4) Does not include the tax and revenue anticipation notes which were outstanding at the close of the indicated fiscal years because sufficient funds had been set aside for the payment of such notes in full prior to the end of said fiscal years.
(5) Tax and revenue anticipation notes.

*Source:* Government Development Bank

The above tables do not reflect the issuance of the 1993 Telephone Authority Bonds.

## PUBLIC CORPORATIONS

In Puerto Rico, many governmental or quasi-governmental functions are performed by public corporations. These are governmental entities of the Commonwealth created by the Legislature but with varying degrees of independence from the central government. Public corporations are generally created to perform a single function or a limited number of related functions. Most public corporations obtain revenues from charges for services or products, but many are subsidized to some extent by the central government. Most public corporations are governed by boards appointed by the Governor with the advice and consent of the Senate, but some public corporations are subsidiaries of departments of the central government. Capital improvements of most of the larger public corporations are financed by revenue bonds under trust agreements or bond resolutions or notes under loan agreements. The following table presents the outstanding bonds and notes of certain of the public corporations as of February 28, 1993 ("notes" as used in this Section is intended to refer principally to certain types of non-bonded debt regardless of maturity). Debt of certain other public corporations is excluded from this table because such debt is payable primarily from the Federal government or is payable from sources other than Commonwealth appropriations or taxes or revenues of public corporations derived from services or products, such as industrial development bonds. Also excluded from this table is the debt of certain public corporations the inclusion of which would reflect double counting. More detailed information about the major public corporations is presented in following sections.

### Outstanding Debt
### February 28, 1993

| | Bonds | | | Notes | | | Total Bonds and Notes | | |
|---|---|---|---|---|---|---|---|---|---|
| | With Guaranty | Without Guaranty | Total | With Guaranty | Without Guaranty | Total | With Guaranty | Without Guaranty | Total |
| | | | | | (In thousands) | | | | |
| Agricultural Services Administration | $ — | $ — | $ — | $ — | $ 50,665 | $ 50,665 | $ — | $ 50,665 | $ 50,665 |
| Aqueduct and Sewer Authority(1) | — | 459,477(2) | 459,477 | — | 215,901 | 215,901 | — | 675,378 | 675,378 |
| Commercial and Agricultural Credit and Development Corporation | — | — | — | — | 107,518 | 107,518 | — | 107,518 | 107,518 |
| Electric Power Authority(1) | — | 2,714,491 | 2,714,491 | — | 110,000 | 110,000 | — | 2,824,491 | 2,824,491 |
| Health Facilities and Services Administration | — | — | — | — | 364,150 | 364,150 | — | 364,150 | 364,150 |
| Highway and Transportation Authority | — | 1,238,635 | 1,238,635 | — | — | — | — | 1,238,635 | 1,238,635 |
| Housing Bank | 91,695 | 575,527(3) | 667,222 | — | 22,620 | 22,620 | 91,695 | 598,147 | 689,842 |
| Industrial Development Company(1) | — | 193,454 | 193,454 | — | 39,609 | 39,609 | — | 233,063 | 233,063 |
| Infrastructure Financing Authority | — | 287,470 | 287,470 | — | — | — | — | 287,470 | 287,470 |
| Maritime Shipping Authority | — | — | — | 60,000 | 248,580(4) | 308,580 | 60,000 | 248,580 | 308,580 |
| Office for the Improvement of Public Schools | — | — | — | — | 122,385 | 122,385 | — | 122,385 | 122,385 |
| Ports Authority | — | 148,520 | 148,520 | — | 27,896 | 27,896 | — | 176,416 | 176,416 |
| Public Buildings Authority(1) | 1,145,249 | — | 1,145,249 | — | 2,133 | 2,133 | 1,145,249 | 2,133 | 1,147,382 |
| Sugar Corporation | — | — | — | — | 157,470 | 157,470 | — | 157,470 | 157,470(3) |
| Telephone Authority | — | 1,043,757 | 1,043,757 | — | 100,185 | 100,185 | — | 1,143,942 | 1,143,942 |
| University of Puerto Rico | — | 195,177 | 195,177 | — | 35,350 | 35,350 | — | 230,527 | 230,527 |
| Others | — | 29,723 | 29,723 | — | 213,380 | 213,380 | — | 243,103 | 243,103 |
| Total | $1,236,944 | $6,886,231 | $8,123,175 | $60,000 | $1,817,842 | $1,877,842 | $1,296,944(5) | $8,704,073 | $10,001,017 |

(1) Does not include accretion of interest from the respective issuance dates on capital appreciation bonds as follows: Aqueduct and Sewer Authority $5,671,627 as of June 30, 1992; Electric Power Authority $45,735,641 as of February 28, 1993; Industrial Development Company $1,709,929 as of February 28, 1993; and Public Buildings Authority $15,004,025; as of February 28, 1993

(2) Principal of and interest on $69,900,000 of this debt is reimbursed from Commonwealth appropriations.

(3) Payable primarily from Commonwealth appropriations

(4) Includes $33,716,000 of capitalized lease obligation

(5) Authorization for Commonwealth guarantees of debt as of February 28, 1993 was $2,285,000,000. Excludes $24,800,000 of loans from private lending institutions to farmers guaranteed by Farm Credit Security Fund as of April 30, 1993.

*Source:* Government Development Bank

No deductions have been made in the above table for debt service funds and debt service reserve funds. The above table does not reflect the issuance of the 1993 Telephone Authority Bonds.

## Government Development Bank for Puerto Rico

The principal functions of Government Development Bank are to act as financial advisor to and fiscal agent for the Commonwealth, its municipalities and public corporations in connection with the issuance of bonds and notes, to make loans and advances to public corporations and municipalities, and to make loans to private enterprises to aid in the economic development of Puerto Rico.

As of February 28, 1993, $2,228,345,000 of bonds and notes of Government Development Bank were outstanding. Government Development Bank has loaned $1,524,214,484 to certain Commonwealth public corporations and municipalities. Act No. 12, approved May 9, 1975, as amended, provides that the payment of principal of and interest on specified notes and other obligations of Government Development Bank, not exceeding $550,000,000, may be guaranteed by the Commonwealth, of which $292,000,000 were outstanding as of February 28, 1993.

Government Development Bank has the following principal subsidiaries and affiliates:

*Higher Education Assistance Corporation* was established in May 1981 for the purpose of guaranteeing loans made to post-secondary school students under Federal insurance programs. It began operations in October 1981 and as of February 28, 1993 had guaranteed 196,099 loans totaling $501,171,331.

*Housing Finance Corporation* was created in November 1977 for the purposes of providing needed rental housing units and stimulating the construction industry under federally subsidized programs. The Corporation has issued tax-exempt revenue bonds and notes to finance the construction of housing units approved for federal rental subsidies, which bonds and notes are limited obligations of the Corporation payable solely from revenues collected in respect of such housing units. The Federal Housing Administration has insured mortgages on certain of the housing units. As of February 28, 1993, $1,611,631,600 of bonds were outstanding.

*Public Finance Corporation* was established in December 1984 for the purpose of providing the agencies and instrumentalities of the Commonwealth with alternate means of meeting their financing requirements. The Corporation issued $400,000,000 of bonds in fiscal 1985 in order to refinance at lower interest rates certain debt of Sugar Corporation that was held by Government Development Bank. On January 3, 1991 and March 14, 1991, the Corporation sold the Sugar Corporation debt and applied the net proceeds of such sales, together with other moneys, to defease and retire all of the outstanding bonds.

## Other Public Corporations

*Aqueduct and Sewer Authority* owns and operates a system of public water supply and sanitary sewer facilities. Capital expenditures are financed by revenues of the system, debt and federal and Commonwealth grants. Debt service on revenue bonds is payable from net revenues of the system. As of February 28, 1993, the Authority had bonds outstanding in the amount of $459,477,000 (not including accretion of interest from the respective issuance dates on capital appreciation bonds) and notes outstanding in the amount of $215,901,000.

Facilities and operations of the Authority's system are subject to regulation under numerous federal and Commonwealth environmental laws, including the Federal Clean Water Act administered by the United States Environmental Protection Agency ("EPA"). The Authority has embarked on an extensive capital improvement program for the five year period ending June 30, 1997 that is estimated to cost approximately $959,000,000. A portion of the capital improvement program is designed to enable the Authority to comply with a series of consent orders agreed to by the Authority and EPA.

*Economic Development Bank* was created in July 1985 to engage primarily in granting small direct loans, providing loan guarantees to private enterprises and making equity investments in such enterprises. Its initial capital was provided by a transfer of loans in the principal amount of $15,000,000 previously administered by a now inactive subsidiary of Government Development Bank. On August 5, 1988, the Economic Development Bank issued $24,000,000 principal amount of Capital Notes payable from Commonwealth appropriations.

*Electric Power Authority* owns and operates the island's electric system. Capital improvements are financed primarily by borrowed funds, supplemented by internally generated funds. The Authority's bonded debt consists of Electric Revenue Bonds and Power Revenue Bonds. Electric Revenue Bonds are secured by a prior lien on net revenues of the electric system. Power Revenue Bonds are payable from such net revenues after provision for debt service and reserve requirements for Electric Revenue Bonds. As of February 28, 1993, the Electric Power Authority had $2,714,491,000 in bonds outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds).

*Health Facilities and Services Administration* was created by Act No. 26, approved on November 13, 1975, as amended, with the objectives of planning, evaluation and development of health services, alleviation of environmental contamination, operation of public hospitals and other health facilities, prevention and treatment of mental illness and administration of family planning programs and maternal and child care activities. The operations of the Administration are funded in part by appropriations from the Commonwealth. The outstanding debt as of February 28, 1993 was $364,150,000.

*Highway and Transportation Authority* is responsible for highway construction in Puerto Rico. Such construction is financed by debt (interim notes and revenue bonds), revenues of the Authority, and federal and Commonwealth grants. Debt service on the Authority's revenue bonds constitutes a first lien on its gross revenues, which consist of all the proceeds of the gasoline tax, one-half of the proceeds of the tax on gas oil or diesel oil, highway toll revenues and the gross receipts of $15.00 per vehicle per year from certain motor vehicle license fees. Such revenues (except for toll revenues) may be applied first to the payment of debt service on general obligation bonds and notes of the Commonwealth and payments required to be made by the Commonwealth under its guarantees of bonds and notes to the extent that no other revenues are available for such purpose. The Commonwealth has never applied such revenues for such payment. As of February 28, 1993, there were outstanding $1,238,635,000 in bonds of the Authority.

The Authority has entered into a concession agreement for the design, construction and operation by a private company of a toll bridge spanning the San José Lagoon to provide an alternate route to Luis Muñoz Marín International Airport. The toll bridge is being financed with the Authority's special facility revenue bonds payable by the private company principally from toll revenues. The concession is for a term of 35 years subject to earlier termination or extension. The bridge is expected to be open for traffic by early 1994. In certain instances as described in the agreement, the Authority may be required, among other things, to assume the private company's obligations with respect to the special facility revenue bonds. The Authority is exploring the possibility of entering into other public-private partnerships for the construction and operation of other traffic facilities.

*Housing Bank and Finance Agency* is engaged in insuring mortgages and servicing mortgages originated by Urban Renewal and Housing Corporation and issues bonds and notes to provide interim and permanent financing for low-income housing projects and single-family home ownership programs. The Agency obtains funds from legislative appropriations, sales of mortgages, mortgage repayments, and other sources.

As of February 28, 1993, the Agency had outstanding $667,222,000 of bonds issued to pay obligations of the Commonwealth under law, otherwise payable from Commonwealth appropriations, to fund certain payments of the Commonwealth under its mortgage subsidy program for low and moderate income families, to guaranty certain insurance obligations of the Agency under certain programs and to refund bonds originally issued by Urban Renewal and Housing Corporation. These bonds are payable principally from appropriations in substantially the amount that the Commonwealth would otherwise have been obligated to appropriate for such purposes.

*Industrial Development Company* participates in the Commonwealth-sponsored economic development program by providing physical facilities, general assistance, and special incentive grants to manufacturers. The Company has issued interim notes and revenue bonds to finance factories and other facilities. Rentals derived from the leasing of specified facilities of the Company are pledged to the payment of the Company's revenue bonds. As of February 28, 1993, the Company had $193,454,000 in bonds outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds).

*Industrial, Medical, Educational and Environmental Pollution Control Facilities Financing Authority* was created in June 1977. The Authority has issued revenue bonds to finance industrial, pollution control, medical and higher education facilities in Puerto Rico for the use of private companies, non-profit entities or government agencies. The bonds are payable solely from payments to be made to the Authority by such private companies, non-profit entities or government agencies and do not constitute a debt of the Commonwealth or any of its other public corporations or municipalities. As of February 28, 1993, $3,057,552,670 of the Authority's bonds had been issued, of which $2,285,955,986 were outstanding.

*Infrastructure Financing Authority* was created in June 1988 for the purpose of providing financial, administrative, consulting, technical, advisory and other types of assistance to other public corporations and governmental instrumentalities of the Commonwealth authorized to develop infrastructure facilities and to establish alternate means for financing infrastructure facilities. The legislation establishes a Puerto Rico Infrastructure Fund funded in the amount of $30 million during fiscal 1989 and $40 million for the following 29 fiscal years with the first proceeds of federal excise taxes imposed on rum and other articles produced in Puerto Rico and sold in the United States which are transferred to the Commonwealth pursuant to the Internal Revenue Code of 1986, as amended. In November 1988 the Authority issued $327,740,000 of Special Tax Revenue Bonds, Series 1988A to refund in advance certain outstanding revenue bonds and other debt of the Aqueduct and Sewer Authority. As of February 28, 1993, $287,470,000 of such bonds were outstanding. The Authority's Special Tax Revenue Bonds, Series 1988A are secured by a pledge of a portion of such federal excise taxes, subject to the rights of the owners of the Commonwealth's general obligation bonds and notes and certain other obligations guaranteed by the Commonwealth.

*Maritime Shipping Authority* commenced operations in 1974 upon the acquisition of three shipping lines serving Puerto Rico and the United States mainland. The Authority acquired vessels and other equipment financed by the issuance of notes on a secured basis to the previous owners. The Authority carries over 40% of the total cargo shipped between Puerto Rico and the United States mainland.

From the commencement of operations through December 27, 1992, the Authority had incurred an accumulated deficit of $214,168,000. The Authority's net loss for the first six months of fiscal 1993 was approximately $5,883,000.

The Commonwealth has appropriated $117,614,000 in past years as capital contributions to the Authority. On July 21, 1988, the Legislature approved a joint resolution to provide an additional capital contribution of $60,000,000 to be paid in six equal annual installments starting in fiscal 1989, of which $50,000,000 has been appropriated. The Commonwealth has undertaken an evaluation of the operations of the Authority to determine the feasibility of privatizing its operations or selling its assets. Additional capital contributions from the Commonwealth may be required to meet its obligations.

During fiscal 1988, the Authority obtained a loan from Government Development Bank to purchase five container ships at a cost of approximately $45,000,000 and to finance in part their refurbishing at a cost of approximately $43,000,000. As of February 28, 1993, the debt of the Authority (including certain capitalized lease obligations) amounted to approximately $308,580,000. Government Development Bank has guaranteed approximately $51,314,000 of such debt. In addition, as of February 28, 1993, the Commonwealth has guaranteed commercial paper of the Authority aggregating $60,000,000.

*Municipal Finance Agency* was created in 1972 as a municipal "bond bank" for Puerto Rico. The Agency has a Board of Directors named by the Governor of the Commonwealth. The President of Government Development Bank is the president of the Agency.

The Agency is authorized to issue bonds to purchase general obligation bonds of Puerto Rico municipalities and the funding of a debt service reserve. Debt service on the Agency's bonds is payable from debt service payments on municipal bonds held by the Agency and from the reserve, including investment income thereof. The Commonwealth has agreed to pay such amounts to the reserve as may be necessary to maintain it at its required level, subject to appropriation by the Legislature, which appropriation is not legally required to be made. To date no such payments have been required.

*Ports Authority* owns and operates major airport and seaport facilities. The Authority derives revenues from a variety of sources, including charges on airplane fuel sales, air terminal space rentals, airline landing fees, wharfage, dockage, and harbor fees, and rentals for the lease of seaport equipment and property. The

Authority's debt consists mainly of revenue bonds $148,520,000 of which were outstanding as of February 28, 1993, which are secured by a pledge of net revenues from most of the Authority's airport and seaport facilities.

*Public Buildings Authority* is authorized to construct, purchase or lease office, school, health, and social welfare facilities for lease to Commonwealth departments, public corporations and instrumentalities. Bonds that have been issued by the Authority to finance such facilities (through retirement of interim notes or otherwise) are payable from lease payments, which are largely derived from Commonwealth appropriations, and are further secured by the Commonwealth's guaranty. The Authority is authorized by Act No. 17 of 1968, as amended, to have outstanding at any one time up to $1,200,000,000 of bonds guaranteed by the Commonwealth. As of February 28, 1993, $1,145,249,000 of such bonds of the Authority were outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds).

The Authority is undertaking a program to construct additional correctional facilities to be completed by the end of fiscal 1997 at an estimated cost of $368,269,075. The program is expected to be financed from appropriations from the General Fund to be reimbursed from general obligation bond proceeds. Through fiscal 1993 $248,645,000 had been appropriated for this purpose.

*Sugar Corporation* was created in 1973 to consolidate ownership and management of the Commonwealth's interests in Puerto Rico's sugar industry. Sugar Corporation owns or leases and operates virtually all the sugar production facilities on the island. Sugar Corporation buys all cane grown by private growers, processes the cane, and sells the crude and refined sugar and molasses.

Puerto Rico's sugar industry has for many years been a deficit operation. From July 1974 to February 28, 1993, the Corporation's cash deficit totaled approximately $863,371,000. The Corporation's objective is to maintain sugar production at 73,200 tons of sugar per year for local consumption only, with any excess being exported to the United States.

On September 23, 1983 the Legislature of Puerto Rico approved Joint Resolution No. 23 which provided a payment plan for the outstanding notes issued by Sugar Corporation to finance prior years cash deficits up to December 31, 1982 and the outstanding debt incurred in the purchase of several sugar mills. $200,000,000 of the outstanding debt as of December 31, 1992 will be paid from future Commonwealth appropriations over a remaining 1½ year period in amounts, including principal and interest. The final appropriation in the amount of $83,250,000 will be made in fiscal year 1994. It is expected that appropriations of up to $30,000,000 per year will be made to cover future annual operating deficits. In order to insure that the annual cash deficit will not exceed $30,000,000, Sugar Corporation is required to present quarterly reports to the Legislature and implement cutbacks if necessary.

On February 28, 1993, the total debt of the Corporation was $157,470,000, including $140,000,000 of Sugar Notes publicly held, $14,704,000 held by private institutions and $2,766,000 of notes held by Government Development Bank.

*Telephone Authority* in July 1974 purchased Puerto Rico Telephone Company from International Telephone and Telegraph Corporation. The Company operates the principal telephone system in Puerto Rico. The Telephone Authority acquired the assets of the Puerto Rico Communications Authority on May 30, 1990. Capital improvements at present are financed by internally generated funds, although in the past they were also financed with revenue bonds. The Authority's revenue bonds are payable from net revenues, which consist primarily of moneys received after payment of the Company's operating expenses. As of February 28, 1993, the Authority had $1,124,762,000 of bonds and other obligations outstanding, none of which was supported by the guaranty of the Commonwealth.

In December, 1992, the Authority sold approximately 80% of its interest in Telefónica Larga Distancia ("TLD") to Telefónica Internacional, a subsidiary of Telefónica de España, for $141.6 million. The gain on the sale will be applied to certain public education purposes, and the balance not so applied will be deposited in the Construction Fund under the Authority's Trust Agreement.

On April 13, 1993, the Authority issued the 1993 Telephone Authority Bonds, including $695,295,000 of bonds to refund most of the outstanding revenue bonds, producing a net present value debt service savings of approximately $158 million.

*University of Puerto Rico,* with approximately 54,450 students, is by far the largest institution of higher education on the island. Commonwealth appropriations are the principal source of University revenues, but additional revenues are derived from tuition, student fees, auxiliary enterprises, interest income, Federal grants and other sources. University capital improvements have been financed mainly by revenue bonds, of which $195,177,000 were outstanding as of February 28, 1993. Revenue bonds are general obligations of the University (which has no taxing power) secured by tuition, student fees, and various other revenue sources.

*Urban Renewal and Housing Corporation* was established to carry out activities related to the provision of low-cost housing for moderate income families, federally aided public housing for low income families, and urban renewal, housing and related activities financed by Commonwealth appropriations. As of February 28, 1993, the Corporation's outstanding debt totalled $307,792,000. On August 9, 1991, the Legislature approved Act No. 55, which dissolved the Corporation and created the Urban Renewal and Housing Corporation Liquidation Office to be administered by a Special Trustee. The Special Trustee has taken control of the assets of the Corporation and is to provide for the total liquidation of the Corporation, including its assets and liabilities. The debt of the Corporation continues to be paid in accordance with their terms. The Act also provided for the Department of Housing to carry on housing programs in the Commonwealth.

In 1964, a fund was organized to enable the Corporation to engage in construction of low-cost housing for moderate income families. It was contemplated that the program would be financed completely by special obligation bonds of the Corporation to be payable in the first instance from mortgage repayments, rentals and other pledged revenues, and to be additionally secured by the guaranty of the Commonwealth. Act No. 18 approved May 7, 1964, as amended, provides for the guaranty by the Commonwealth of the payment of principal of and interest on an amount not exceeding $325,000,000 of such bonds, of which $171,000,000 have been issued and $91,695,000 were outstanding as of February 28, 1993. These bonds were assumed by the Housing Bank and Finance Agency on May 14, 1992.

As of said date, additional debt issued by the Corporation to finance the program consisted of $206,987,000 of bonds which are paid mainly by Commonwealth appropriations and have been assumed by the Housing Bank and Finance Agency. Annual debt service on these bonds related to the low cost housing program is payable from Commonwealth appropriations of up to $30,949,000 per year. These appropriations would be reduced to the extent that revenues derived from the low-cost housing program exceed debt service on the Corporation's special obligation bonds referred to above and from other internally generated funds. The amount appropriated in the current fiscal year amounts to $22,619,000.

*Public corporations* in addition to those mentioned above have issued debt in the aggregate amount of $518,851,000 as of February 28, 1993. Debt service on $87,948,000 of such outstanding debt is being paid from Commonwealth appropriations. However, the Commonwealth is not obligated to make any such appropriations. Additional appropriations are made by the Commonwealth to enable certain of such corporations to pay their operating expenses.

## INSURANCE MATTERS

In December 1992, the property and casualty insurance company that insured approximately $5 billion of Commonwealth-owned property was placed in court-ordered liquidation, thus requiring the Commonwealth to seek alternate insurance arrangements for certain properties and major structures which currently are uninsured to protect against losses from fire, hurricane or other natural disasters, and personal liability. There is no assurance that alternate insurance arrangements can be secured for all of these properties and structures or that the arrangements made will provide full insurance coverage to the Commonwealth. The Commonwealth is exploring options, which include, among others, the formation of a captive insurance company, to address its insurance needs. Personal injury awards against the Commonwealth are limited by law to $150,000 per occurrence.

## RETIREMENT SYSTEMS

Public employees of the Commonwealth and its instrumentalities are covered by five retirement systems: the Employees Retirement System of the Government of Puerto Rico and its Instrumentalities (the "Employees Retirement System"), the Annuity and Pension System for the Teachers of Puerto Rico (the "Teachers Retirement System"), the Commonwealth of Puerto Rico Judiciary Retirement System (the "Judiciary Retirement System"), the Retirement System of the University of Puerto Rico (the "University Retirement System"), and the Employees Retirement System of Puerto Rico Electric Power Authority (the "Electric Power Authority Retirement System").

The University Retirement System and the Electric Power Authority Retirement System apply, respectively, to employees of the University of Puerto Rico and Puerto Rico Electric Power Authority. The Commonwealth is not required to contribute directly to those two systems, but a large proportion of University revenues are derived from central government appropriations.

The Teachers Retirement System covers public school teachers, the Judiciary Retirement System covers judges, and the Employees Retirement System covers all other employees of the Commonwealth and its municipalities and instrumentalities. As of June 30, 1992, the total number of active members of the three systems was as follows: Employees Retirement System, 156,230; Teachers Retirement System, 45,169,000 and Judiciary Retirement System, 262. These three systems are financed by contributions by the employers (the Commonwealth, public corporations or municipalities), employees, and investment income. The Commonwealth is responsible for approximately 66% of total employer contributions to the Employees Retirement System and 100% and 93% of total employer contributions to the Judiciary and Teachers Retirement Systems, respectively. Retirement and related benefits provided by the systems and required contributions to the systems by employees are determined by statute. Required contributions to the systems by employers are determined by statute with respect to the Teachers Retirement System and, with respect to the Employees and Judiciary Retirement Systems, by the Administrator of the Systems. In fiscal 1993, the Commonwealth has budgeted approximately $179,178,000 as its contribution to the Employees Retirement System, $2,911,000 as the contribution to the Judiciary Retirement System and $65,716,000 as its contribution to the Teachers Retirement System.

The most recent actuarial valuation of the Employees Retirement System and Judiciary Retirement System was submitted by a firm of independent consulting actuaries in June 1989 and updated as of June 30, 1990. As of June 30, 1990, the total pension benefit obligation for the Employees Retirement System and Judiciary Retirement System was $4,300,000,000 and $46,500,000, respectively. The unfunded pension benefit obligation of the Employees Retirement System and Judiciary Retirement System for the same period was $3,536,222,000 and $17,754,000, respectively. The actuarial valuation was done in accordance with the "Projected Unit Credit" method. An investment return of 9% per year, a salary increase of 6% per year and a post retirement benefit increase for the Employees Retirement System of 3% every third year were assumed. This benefit increase was provided by the Legislature of Puerto Rico, on May 10, 1992, by Act No. 10. The first 3% increase was granted to retirees who have been receiving their annuities for three or more years as of that date. Subsequent increases will depend upon the explicit approval of the System's Board of Trustees and the Legislature, based on a favorable recommendation from the System's independent consulting actuary and given a minimum of 24 months of benefit payment reserves.

The Legislature of Puerto Rico, on February 1, 1990, enacted Act No. 1 which is directed at ensuring the solvency of the Employees Retirement System for the next fifty years. Among other provisions, the legislation increases the level of contribution to the System and limits benefits for new employees by increasing the length of time for the vesting of certain benefits and reducing the level of benefits in the case of early retirement. The legislation also reduces the level of occupational injury and death benefits received by new employees.

The most recent actuarial valuation of the Teachers Retirement System was submitted by a firm of independent consulting actuaries in March 1992. As of June 30, 1990 the total pension benefit obligation of the system was $1,997,100,000, assets amounted to $969,500,000 and the resulting unfunded pension benefit obligation was $1,027,600,000.

It is recognized that it will be necessary to strengthen the finances of the Teachers Retirement System in order to assure that combined contributions and investment income continue to exceed benefit payments, avoiding the possible future drawdown of assets.

The following table presents in summary form income and expenses of the retirement systems for the fiscal years ended June 30, 1991 and 1992 and estimates for the fiscal year ending June 30, 1993.

**Retirement Systems**

**Income and Expenses**

| | Employees Retirement System | Judiciary Retirement System | Teachers Retirement System |
|---|---|---|---|
| | | (in thousands) | |
| **Fiscal Year Ended June 30, 1991** | | Actual | |
| Income: | | | |
| Employers contributions | $167,476 | $2,363 | $ 53,055 |
| Employee contributions | 129,991 | 972 | 44,318 |
| Investment income | 69,607 | 2,821 | 105,729 |
| Total | $367,074 | $6,156 | $203,102 |
| Expenses: | | | |
| Benefit payments | $269,641 | $3,892 | $107,589 |
| Administrative and other expenses | 14,048 | 401 | 15,840 |
| Total | $283,689 | $4,293 | $123,429 |
| Net Income | $ 83,385 | $1,863 | $ 79,673 |
| **Fiscal Year Ended June 30, 1992** | | Preliminary | |
| Income: | | | |
| Employers contributions | $179,024 | $2,548 | $ 61,812 |
| Employee contributions | 138,593 | 1,041 | 45,454 |
| Investment income | 93,962 | 4,131 | 92,765 |
| Total | $411,579 | $7,720 | $200,021 |
| Expenses: | | | |
| Benefit payments | $291,467 | $4,306 | $131,024 |
| Administrative and other expenses | 14,716 | 310 | 6,200 |
| Total | $306,182 | $4,616 | $137,224 |
| Net Income | $105,397 | $3,104 | $ 62,797 |
| **Fiscal Year Ending June 30, 1993** | | Estimated | |
| Income: | | | |
| Employers contributions | $179,178 | $2,911 | $ 65,716 |
| Employee contributions | 140,751 | 1,233 | 47,326 |
| Investment income | 69,714 | 3,669 | 102,696 |
| Total | $389,643 | $7,813 | $215,738 |
| Expenses: | | | |
| Benefit payments | $305,632 | $4,596 | $140,357 |
| Administrative and other expenses | 15,958 | 181 | 7,105 |
| Total | $321,590 | $4,777 | $147,462 |
| Net Income | $ 68,053 | $3,036 | $ 68,276 |

*Sources:* Employees Retirement System, Judiciary Retirement System and Teachers Retirement System

## SUMMARY OF COMMONWEALTH FINANCIAL STATEMENTS

The Department of the Treasury has completed the conversion of the accounting and financial reporting system of the Central Government to generally accepted accounting principles for governmental entities (GAAP). Fiscal 1989 was the first year for which the Commonwealth's financial statements were prepared in accordance with generally accepted accounting principles, and the balance sheet was audited by KPMG Peat Marwick. For fiscal 1990 and 1991 the complete financial statements of the Commonwealth have been audited by KPMG Peat Marwick, whose report thereon for fiscal 1991 is set forth in *Appendix II*. The financial statements of the Commonwealth for fiscal year 1992 are being audited by KPMG Peat Marwick and are expected to be available in June 1993. Preparation of the audited financial statements of the Commonwealth involves the collection and consolidation of audited financial statements from 55 separate reporting entities. The financial statements for fiscal years after fiscal 1988 differ from previous fiscal years' financial statements of the Commonwealth because of the inclusion of the public corporations within the reporting entity.

Reference is made to *Appendix II* for the General Purpose Financial Statements of the Commonwealth for the fiscal year ended June 30, 1991.

## COMMONWEALTH TAXES, OTHER REVENUES AND EXPENDITURES

The Secretary of the Treasury has custody of the funds of the Central Government of the Commonwealth and is responsible for the disbursement and investment of and accounting for such funds. Central government funds are grouped into three major categories or "types" of funds, as follows: (i) Governmental Fund Types, which include the General, Special Revenue, Debt Service (also referred to herein as Redemption), and Capital Project Funds; (ii) Proprietary Fund Types, which include the Enterprise and Internal Service Funds; and (iii) Fiduciary Fund Types, which include the Trust and Agency Funds. These funds do not include funds of the municipalities, because the municipalities are governmental entities with independent treasuries.

The General Fund is the primary operating fund of the Commonwealth. General Fund revenues are broadly based and include revenues raised internally as well as those from non-Commonwealth sources. Internal revenues consist principally of income taxes and excise taxes. Revenues from non-Commonwealth sources are derived from federal excise taxes and customs duties returned to the Commonwealth. The primary expenditures of the Commonwealth through the General Fund are for grants and subsidies and personal and other services.

### Summary and Management Discussion of General Fund Results

The following table presents the Commonwealth revenues and expenditures of the General Fund on a cash basis for fiscal 1988 through fiscal 1993. Insofar as the information relates to April through June of fiscal 1993, it is based on estimates provided by the Secretary of the Treasury. The information for fiscal 1988 through fiscal 1992 and for the first nine months of 1993 is based on actual year end or month end results. Starting with fiscal 1989, General Fund revenues, expenditures and transfers as presented in the table differ from the General Fund revenues, expenditures and transfers as presented in the financial statements included in *Appendix II*, as the latter statements reflect an expanded General Fund entity in accordance with generally accepted accounting principles.

## Commonwealth of Puerto Rico
## General Fund Revenues, Expenditures, and Changes in Cash Balance

| | Fiscal Year | | | | | |
|---|---|---|---|---|---|---|
| | 1988 | 1989 | 1990 | 1991 | 1992(1) | 1993(2) |
| | (in thousands) | | | | | |
| Beginning cash balance | $ (87,884) | $ 190,257 | $ 173,943 | $ 112,251 | $ 105,475 | $ (62,359) |
| Revenues from internal sources: | | | | | | |
| Income taxes: | | | | | | |
| Individuals | 1,011,824 | 868,976 | 1,030,458 | 1,129,185 | 1,142,154 | 1,235,000 |
| Corporations | 736,257 | 786,880 | 849,313 | 931,912 | 1,019,468 | 976,000 |
| Partnerships | 7,478 | 5,034 | 2,119 | 4,001 | 1,167 | 1,050 |
| Withheld from non-residents | 84,022 | 46,366 | 53,439 | 48,312 | 62,066 | 52,000 |
| Tollgate taxes | 119,841 | 118,751 | 100,253 | 176,851 | 98,502 | 120,000 |
| Interest | 12,302 | 10,910 | 16,819 | 15,060 | 8,505 | 6,000 |
| Dividends | 22,846 | 20,531 | 26,428 | 25,644 | 23,588 | 28,000 |
| Total income taxes | 1,994,570 | 1,857,448 | 2,078,829 | 2,330,965 | 2,355,450 | 2,418,050 |
| Commonwealth excise taxes: | | | | | | |
| Alcoholic beverages | 184,146 | 182,466 | 222,184 | 219,055 | 216,890 | 214,000 |
| Cigarettes | 98,593 | 97,890 | 113,809 | 104,454 | 102,400 | 104,000 |
| Motor vehicles | 180,579 | 194,875 | 188,814 | 172,272 | 178,329 | 200,000 |
| Other excise taxes | 428,622 | 440,869 | 433,691 | 429,235 | 490,396 | 509,000 |
| Total Commonwealth excise taxes | 891,940 | 916,100 | 958,498 | 925,016 | 988,015 | 1,027,000 |
| Property taxes | 160,335 | 100,269 | 112,929 | 132,375 | 0 | 0 |
| Inheritance and gift taxes | 3,000 | 3,000 | 820 | 1,421 | 1,147 | 1,000 |
| Licenses | 52,593 | 44,103 | 40,523 | 38,690 | 48,135 | 48,000 |
| Other: | | | | | | |
| Lottery | 60,935 | 67,520 | 74,416 | 64,563 | 60,597 | 63,000 |
| Electronic Lottery | 0 | 0 | 0 | 0 | 59,091 | 54,000 |
| Miscellaneous non-tax revenues | 99,633 | 92,435 | 167,972 | 168,137 | 111,148 | 104,000 |
| Total other | 160,568 | 159,955 | 242,388 | 232,700 | 230,836 | 221,000 |
| Total revenues from internal sources | 3,263,006 | 3,080,875 | 3,433,987 | 3,661,167 | 3,623,583 | 3,715,050 |
| Revenues from non-Commonwealth sources: | | | | | | |
| Federal excise taxes | 188,000 | 177,965 | 213,714 | 199,386 | 196,498 | 180,000 |
| Customs | 103,060 | 105,355 | 93,659 | 94,384 | 93,038 | 95,000 |
| Total revenues from non-Commonwealth sources | 291,060 | 283,320 | 307,373 | 293,770 | 291,536 | 275,000 |
| Total revenues | 3,554,066 | 3,364,195 | 3,741,360 | 3,954,937 | 3,915,119 | 3,990,050 |
| Transfers to debt service fund(4) | (190,872) (3) | (215,000) (3) | (244,806) | (273,859) | (283,236) | (295,881) |
| Revenues from 1992 tax amnesty | 0 | 0 | 0 | 0 | 189,877 | 0 |
| Other non-revenue sources | 0 | 0 | 161,000 (5) | 30,000 (6) | 0 | 0 |
| Note proceeds(7) | 430,275 | 529,220 | 650,391 | 400,236 | 0 | 401,917 |
| Repayment of notes(8) | (446,202) | (544,354) | (664,202) | (408,120) | 0 | (413,788) |
| Adjusted revenues | 3,347,267 | 3,134,061 | 3,643,743 | 3,703,194 | 3,821,760 | 3,682,298 |
| Expenditures: | | | | | | |
| Grants and subsidies | 1,461,163 | 1,776,585 | 1,234,333 | 1,197,664 | 1,217,157 | 1,217,236 |
| Personal services | 1,121,969 | 1,249,764 | 1,295,561 | 1,332,459 | 1,405,472 | 1,413,610 |
| Other services | 353,312 | 402,757 | 371,745 | 348,237 | 448,239 | 420,630 |
| Materials and supplies | 52,302 | 72,875 | 64,886 | 60,118 | 67,474 | 63,780 |
| Equipment purchased | 27,472 | 48,577 | 32,949 | 26,834 | 31,152 | 42,567 |
| Capital outlays | 23,711 | 19,382 | 31,888 | 50,490 | 41,235 | 22,117 |
| Debt Service on special promissory notes and GDB lines of credit | 5,198 | 0 | 0 | 74,354 | 63,891 | 5,783 |
| Total expenditures | 3,045,127 | 3,569,940 | 3,031,362 | 3,090,156 | 3,274,620 | 3,185,723 |
| Adjusted revenues less expenditures | 302,140 | (435,879) | 612,381 | 613,038 | 547,140 | 496,575 |
| Transfers: | | | | | | |
| Transfers in and other sources | 196,824 | 590,855 | 176,464 | 441,326 | 515,040 | 562,000 |
| Transfers out and other uses | (220,823) | (171,290) | (850,537) | (1,061,140) | (1,230,014) | (1,200,250) |
| Net transfers | (23,999) | 419,565 | (674,073) | (619,814) | (714,974) | (638,250) |
| Ending cash balance | $ 190,257 | $ 173,943 | $ 112,251 | $ 105,475 | $ (62,359) | $ (204,034) |

(1) Subject to adjustment
(2) Estimated
(3) Does not include amounts deposited directly to the debt service fund from non-General Fund revenues
(4) Consists of amounts to pay principal of and interest on general obligation bonds and notes of the Commonwealth and bonds of the Sugar Corporation of Puerto Rico for which the guarantee of the Commonwealth had been exercised (all such bonds of the Sugar Corporation matured on July 1, 1989). Does not include amount deposited directly to the debt service fund from non-General Fund revenues.
(5) Consists of the sale of assets of the Communications Authority to the Telephone Authority and the release of certain reserves of the Public Buildings Authority
(6) Consists of moneys received by the Commonwealth from the reoffering of certain notes of the Puerto Rico Sugar Corporation
(7) Consists of proceeds from Commonwealth tax and revenue anticipation notes issued in each such fiscal year. In addition, fiscal year 1990 includes $100,000,000 in proceeds under a line of credit provided by Government Development Bank.
(8) Consists of repayment of Commonwealth tax and revenue anticipation notes in each such fiscal year and in fiscal year 1990 of a $100,000,000 line of credit provided by Government Development Bank

Source: Department of the Treasury

*Estimated Fiscal 1993 Compared to Preliminary Fiscal 1992*

General Fund estimated total revenues for fiscal 1993 are forecast at $3,990 million, an increase of $74.9 million (1.9%) over fiscal 1992. Major projected changes are the following: total income taxes increased by $62.6 million, excise taxes by $39.0 million and federal excise taxes are reduced by $18.5 million.

Beginning in fiscal 1992, municipal property taxes are no longer revenues of the General Fund. This revenue source was transferred to the municipalities pursuant to Act. No. 80, approved on August 30, 1991 ("Act No. 80").

In general terms, the revenue increase for fiscal 1993 is tied to the economic expansion projected for fiscal 1993. The economy of the Commonwealth of Puerto Rico is expected to grow at a real rate of 2.9% for fiscal 1993.

Total projected expenditures for fiscal 1993 are expected to decrease to $3,185.7 million, a 2.7% decrease, when compared to preliminary fiscal 1992. Transfers in and transfers out are projected to be maintained at fiscal 1992 levels. The ending cash balance for the General Fund for fiscal 1993 is forecast to decrease by $141.7 million as compared with fiscal 1992

*Preliminary Fiscal 1992 Compared to Fiscal 1991*

Total revenues for fiscal 1992 were 1.0% below fiscal 1991. This was due to the transfer of municipal property taxes to the municipalities under Act No. 80. Although this was partly offset by minor increases in income taxes, excise taxes and licenses, there were slight decreases in revenues from customs duties and federal excise taxes. Excluding municipal property taxes, revenues from internal sources for fiscal 1992 ($3,623 million) increased by 2.7% when compared to fiscal 1991 ($3,529 million). The ending cash balance for the General Fund for fiscal 1992 decreased by $167.8 million as compared with fiscal 1991.

Total expenditures for fiscal 1992 were $3,274.6 million, compared with $3,090.2 million for fiscal 1991. The major component of transfers out during both fiscal year 1992 and 1991 is the amount appropriated from the General Fund to the Health Fund that amounted to $523.6 million in fiscal 1992 and $482.6 in fiscal 1991.

*Fiscal 1991 Compared to Fiscal 1990*

For fiscal 1991, total revenues rose by $212 million to a level of $3,955 million (a 5.7% increase) while total expenditures increased marginally to a level of $3,090 million from $3,031 million. The ending cash balance of the General Fund for fiscal 1991 decreased by approximately $6.8 million as compared with fiscal 1990. The major components of the changes in revenues and expenditures for fiscal 1991 are set forth below.

Total income tax receipts for fiscal 1991 exceeded fiscal 1990 receipts by over $252 million. This increase in total income tax receipts was due in large measure to the growth in the taxpayer base.

Commonwealth excise taxes for fiscal 1991 were lower than fiscal 1990 collections by $33.4 million as a result of a decrease in cigarette, motor vehicle and the five per cent general tax collections.

Non-Commonwealth revenues for fiscal 1991 reflect a reduction of $13.7 million when compared to fiscal 1990. This reduction was due to the $1.00 per barrel increase in federal excise tax (which is not returned to Puerto Rico). In addition, states approved legislation making 21 the minimum age for the consumption of liquor which affected consumption of alcoholic beverages and in turn, revenues for this item.

*Fiscal 1990 Compared to Fiscal 1989*

For fiscal 1990 total revenues rose by $377 million to a level of $3,741 million (an 11.2% increase), while total expenditures declined by $538.6 million to a level of $3,031 million (a 15.1% decrease). The ending cash balance of the General Fund for fiscal 1990 declined by $61.7 million as compared with fiscal 1989. The major components of the changes in revenues and expenditures for fiscal 1990 are set forth below.

Total income tax receipts for fiscal 1990 exceeded fiscal 1989 receipts by over $221.3 million and exceeded the receipts in fiscal 1988, when most tax amnesty revenues were received. This increase in total income tax receipts was due in large measure to the postponement of the final stage of the tax reform program enacted in 1987 and to growth in the taxpayer base.

Commonwealth excise taxes for fiscal 1990 exceeded fiscal 1989 collections by $42.4 million as a result of growth in the economy, while lottery receipts rose by $6.9 million in spite of a temporary disruption in lottery operations in the early part of fiscal 1990.

Non-Commonwealth revenues for fiscal 1990 exceeded fiscal 1989 collections by $24 million, due in large measure to improvements in the collection of federal excise taxes on rum that are rebated to Puerto Rico.

The decline in grants and subsidies for fiscal 1990 over fiscal 1989 arose primarily from increased control of special appropriations by the Treasury and a change in the presentation of payments provided to the Health Facilities and Services Administration. Since fiscal 1990, these payments have been reported as a transfer out rather than as grants and subsidies.

*Fiscal 1989 Compared to Fiscal 1988*

In fiscal 1989, the ending positive cash balance of the General Fund was $173.9 million, compared with an ending positive cash balance for fiscal 1988 of $190.2 million.

Total revenues for fiscal 1989 were $3,364 million compared with $3,554 million for fiscal 1988. The fiscal 1988 revenues include $294.9 million collected during the one-time tax amnesty enacted in 1987 as part of the tax reform program. The fiscal 1989 revenues were negatively affected, as anticipated, by a reduction in income tax collections resulting from the tax reform program. Of the $294.9 million tax amnesty collections in fiscal 1988, $16.4 million were actually disbursed in fiscal 1988, with the balance carried forward to the beginning cash balance for fiscal 1989. During fiscal 1989, $255.4 million were disbursed.

Total expenditures for fiscal 1989 increased by $524 million, due mainly to an increase of $315 million in grants and subsidies and an increase of $128 million in personal services expenditures. Grants and subsidies and personal services increased primarily as a result of increased disbursements to the central government for salaries under the control of the Office of Budget and Management paid to public employees, subsidies to the University of Puerto Rico and municipalities and contributions for operating expenses of the Health Facilities and Services Administration. This increase in grants and subsidies was funded in part from the revenues collected during the fiscal 1988 tax amnesty and the disbursement of additional resources carried forward to fiscal 1989 from previous years. Expenditures for personal services increased by $128 million in fiscal 1989, an 11% increase over fiscal 1988.

Transfers into the General Fund were $590.9 million and transfers out were $171.1 million.

**Major Sources of General Fund Revenues**

*Income Taxes*

The Commonwealth's income tax law, the Income Tax Act of 1954 (the "ITA"), imposes a tax on the income of individual residents of Puerto Rico, trusts, estates, and domestic and foreign (if engaged in a trade or business in Puerto Rico) corporations and partnerships. A withholding tax is imposed on certain payments made to non-residents of Puerto Rico. In October 1987, the ITA was amended as part of a major tax reform program that included a revised excise tax law and a one-time tax amnesty. In order to help cover a projected shortfall in revenues for fiscal 1990, the ITA was further amended in December 1989 to postpone for one year the third year of the three-year reform program. As part of the Commonwealth budget for fiscal 1991, the legislature has approved a modification to the third phase of the tax reform program.

*Individuals.* Resident individuals are subject to tax on their taxable income from all sources. Prior to the tax reform amendments, the tax rates for individuals ranged from 10.26% to 50%. The 1987 tax reform amendments consolidated fifteen tax brackets into four, with rates of 9%, 15%, 25% and 33% subject to a three-year phase-in period commencing in 1988. The 1987 tax reform program provided for maximum individual rates of 41%, 38% and 33%, respectively, for 1988, 1989 and 1990. The 1989 amendments to the ITA extended the phase-in period for an additional year, with the maximum individual rate for 1989 and 1990 at 38%. On April 19,1990, the third phase was modified to provide for a maximum tax bracket reduction to 36% for 1991 and subsequent years, instead of 33% as originally enacted. Individuals with adjusted gross income ("AGI") of $75,000 or more must pay the higher of the regular income tax and an alternative base tax at a rate of 10%, 15% or 20% based on the level of AGI. As a result of the tax reform, the tax-free income level increased from less than $900 to $3,300 for a single individual and from $4,000 to $8,600 for a married couple with two dependents. In addition, certain deductions and exclusions were repealed, phased out or limited. These changes were effective for taxable years commencing after December 31, 1987. Individuals, however, may elect to determine their tax liability with respect to any taxable year commencing on or before December 31, 1992 under the rules that applied prior to the tax reform.

Interest income in excess of $2,000 (the first $2,000 exempt) on deposits with Puerto Rico financial institutions is taxed at a rate of 17%, and dividend income from Puerto Rico sources is taxed at a rate of 20%. Gain realized from the sale or exchange of a capital asset, if held for more than six months, is taxed at a maximum rate of 20%.

*Corporations and Partnerships.* Puerto Rico corporations and partnerships are subject to tax on income from whatever source; foreign corporations and partnerships that are engaged in a trade or business in Puerto Rico are subject to tax on their income from Puerto Rico sources and on income from sources outside Puerto Rico that is effectively connected with the conduct of a trade or business in Puerto Rico. Unless a corporation or partnership qualifies for partial exemption from corporate income and other taxes under the industrial incentives program (see "Tax Incentives" under *The Economy in Appendix I*), it is subject to tax at graduated rates.

The 1987 tax reform amendments reduced the income tax brackets for corporations and partnerships to six, with a reduction in tax rates being phased in over a six-year period commencing in 1988. The 1989 amendments to the ITA postponed the phase-in of the reduction in tax rates indefinitely. The ITA, as amended in 1989, provides for the highest rate applicable to taxable income in excess of $275,000 to be maintained at 42% for taxable years commencing after December 31, 1990. Certain corporations and partnerships covered by Act No. 8 of the Legislature of Puerto Rico, approved January 24, 1987 (known as the Puerto Rico Tax Incentives Act), or by Act No. 52 of the Legislature of Puerto Rico, approved June 2, 1983 (known as the Puerto Rico Tourism Incentives Act), will continue to be subject to a maximum tax rate of 45% on their taxable income. The 1987 amendments also created a new alternative minimum tax of 22%.

The 1987 tax reform amendments created a branch profits tax applicable to resident foreign corporations. The tax is 25% (10% on hotel, manufacturing or shipping operations) of an annual Dividend equivalent amount, and it applies without regard to the Puerto Rico source of income rules.

Most changes affecting corporations were applied to taxable years commencing after December 31, 1986.

Dividends and interest from Puerto Rico sources paid to non-resident corporate recipients generally are subject to a withholding tax at rates of 25% and 29%, respectively. The basic tax on dividends paid to foreign corporate shareholders of United States corporations operating under Section 936 of the Code is 10% but is subject to reduction with respect to dividends paid from profits invested in certain eligible instruments for specified periods of time.

*Excise Taxes*

The revised Excise Tax Act included in the tax reform program imposes a tax on articles and commodities that are imported into or manufactured in Puerto Rico for consumption in Puerto Rico and a tax on certain transactions, such as hotel occupancy, public shows, and horse racing. The excise tax on certain articles and commodities, such as cigarettes and petroleum products, is based upon the quantity of goods imported. The excise tax on motor vehicles is based on horsepower and weight. Under the previous Excise Tax Act, other articles and commodities were divided into nine categories and taxed at different rates, ranging from 2% to 26%, on their "taxable price in Puerto Rico", which, for importers, was generally the F.O.B. factory price. The revised Excise Tax Act imposes a tax at an effective rate of 6.6% of the F.O.B. factory price for imported goods and 3.6% of the sales price of goods manufactured in Puerto Rico, except sugar, cement, cigarettes, motor vehicles and certain petroleum products which are taxed at different rates. The revised Excise Tax Act eliminates the exemption applicable to goods to be used by the government, except for motor vehicles and construction equipment. Exemptions apply to certain articles, such as food and medicines, and to articles designated for certain users.

*Property Taxes*

Personal property, which accounts for approximately 37% of total assessed valuation of taxable property, is self-assessed. No real property reassessment has been made since 1958, and construction taking place after that year has been assessed on the basis of what the cost of construction would have been in 1958. Accordingly, the overall assessed valuation of real property for taxation purposes is substantially lower than the actual market value. Also, an exemption on the first $15,000 of assessed valuation in owner-occupied residences is available.

On August 30, 1991, legislation was adopted in the Commonwealth providing a municipal reform program which involves the creation of a new agency assigned to collect property taxes. The program transfers the previous functions of the Department of the Treasury with respect to real and personal property tax assessment, notification, determination and collection to the new agency. Special provisions have been made so that $1.03 per $100 of property tax collections shall continue to be deposited in the Redemption Fund.

**Commonwealth of Puerto Rico**

**Assessed Valuations and Real and Personal Property Taxes**
**(Commonwealth and Municipalities Combined)**
**(in thousands)**

| Fiscal Year Ended June 30 | Assessed Valuations(1) | Taxes Levied | Collections of Current Year | Collections of Previous Years | Total Collections |
|---|---|---|---|---|---|
| 1987 | $ 9,264,372 | $290,135 | $232,504 | $45,079 | $277,583 |
| 1988(2) | 10,036,999 | 319,733 | 261,167 | 27,509 | 288,676 |
| 1989 | 10,476,743 | 340,020 | 250,184 | 32,074 | 282,258 |
| 1990 | 10,810,982 | 350,700 | 272,370 | 36,912 | 309,282 |
| 1991(3) | 11,359,276 | 374,834 | 275,603 | 76,015 | 351,618 |
| 1992 | 11,209,804 | 368,209 | 276,185 | 22,234 | 298,419 |
| 1993 | 11,337,421 | 373,681 | N.A.(4) | N.A.(4) | N.A.(4) |

(1) Valuation set as of January 1 of preceding fiscal year

(2) Excludes $62,300,000 of property taxes collected during the tax amnesty that expired on February 29, 1988.

(3) Act No. 80, approved by the Puerto Rico Legislature on August 30, 1991, created the Municipal Revenues Collection Center, transferring to this entity the functions and duties of the Department of Treasury regarding the appraisal, notice of imposition and determination and collection of municipal property taxes.

(4) Not available

*Source:* Department of the Treasury

*Other Taxes and Revenues*

Motor vehicle license plate and registration fees comprise the major portion of license tax receipts.

Non-tax revenues consist principally of lottery proceeds, documentary stamps, permits, fees and forfeits, proceeds of land sales and receipts from public corporations in lieu of taxes.

Revenues from non-Commonwealth sources include customs duties collected in Puerto Rico and excise taxes on shipments of alcoholic beverages from the island to the mainland United States. The customs duties and excise taxes on shipments are imposed and collected by the United States and returned to the Commonwealth.

**Collections of Income, Excise and Property Taxes**

The Department of the Treasury has continued its program for improving tax collections which began in fiscal 1986. The program has consisted, in part, of taking the initiative in sponsoring and implementing tax reform, particularly in the areas of excise taxes and income taxes, in order to decrease the incidences of nonpayment of taxes and to expand the taxpayer base. The program has also included (a) improving the methods by which delinquent taxpayers are identified, primarily through the use of computer analyses, (b) computerizing the processing of tax returns, and (c) identifying and eliminating taxpayer abuses of the existing tax laws.

**Transfers to General Obligation Debt Service Fund**

These consist of transfers from the General Fund to the Debt Service Fund for the amortization of the principal of and interest on general obligation bonds and notes of the Commonwealth and bonds issued by the Sugar Corporation for which the guaranty of the Commonwealth had been exercised (all such bonds of the Sugar Corporation matured on July 1, 1989).

**Components of General Fund Expenditures**

*Grants and Subsidies*

This category includes grants and contributions to municipalities, public corporations with independent treasuries and contributions to charitable institutions. It also includes items for or included in court awards, damage awards for personal injury or property damage as well as payment of taxes and payment in lieu of taxes.

*Personal Services*

This category includes compensation paid for personal services rendered to the Commonwealth and its public instrumentalities by individuals or firms in the form of salaries, wages, per diems, fees, commissions or other forms of compensation.

*Other Services*

This category includes the payment of services other than the services referred to above, including advertising, printing, communication services, legal expenses, utility services, building and equipment rental and maintenance expenses, insurance premiums and miscellaneous services.

*Materials and Supplies*

This category includes all articles which ordinarily have short life and durability, lose their characteristic identity in the process of use, have only nominal value ($25 or less), or are not otherwise chargeable as equipment.

*Equipment Purchases*

The category includes items which have three special characteristics which distinguish them from materials; durability, long useful life and high unit cost. In addition, these items are subject to centralized inventory control as fixed assets.

*Capital Outlays*

This category includes the acquisition of land and interests in land, the construction of buildings, roads and bridges, and other structures, as well as permanent improvements and additions.

*Debt Service for Special Promissory Notes and GDB Line of Credit*

Includes payments for the amortization of the principal of and interest on non-general obligation special promissory notes to be paid from collections of past due taxes and, if necessary, from Commonwealth appropriations received in and after fiscal 1990 and payments on notes to GDB to be paid from the balance in the General Fund.

**Transfers**

*Transfers In and Other Sources*

Includes repayment of loans and advances to other funds, certain refunds, advances from other funds and other receipts.

*Transfers Out and Other Uses*

Includes refunds, advances, repayment of advances from other funds, grants and contributions to other funds under the custody of the Secretary of the Treasury and other items. The major portion of transfers out in recent fiscal years consists of transfers to the Health Fund and advances to the municipalities.

**Federal Grants**

The Commonwealth receives federal grants under numerous programs. The following table presents revenues from federal grants by broad program areas which are accounted in the central accounting system of the Treasury Department.

**Commonwealth of Puerto Rico**

**Federal Grants**

| | Fiscal Year Ended and Ending June 30 | | | | |
|---|---|---|---|---|---|
| | 1990 | 1991 | 1992 | 1993(p) | 1994(1) |
| | | | (in thousands) | | |
| Education | $301,339 | $373,975 | $437,695 | $479,345 | $483,436 |
| Social services | 149,507 | 156,322 | 202,522 | 214,849 | 217,229 |
| Health(2) | 22,918 | 26,104 | 24,048 | 23,218 | 22,906 |
| Labor and human resources(3) | 46,198 | 44,744 | 45,341 | 39,687 | 40,608 |
| Public works and transportation | 49,833 | 47,122 | 55,991 | 56,590 | 55,483 |
| Public Safety | 3,256 | 8,658 | 8,114 | 7,507 | 7,307 |
| Housing(4) | 77,088(5) | 12,636(5) | 38,786(6) | 39,875(6) | 45,001(6) |
| Drug Addiction Treatment | 13,589 | 20,957 | 19,845 | 20,643 | 19,460 |
| Emergency assistance(7) | 29,639 | 35,356 | 14,166 | 0 | 0 |
| Other | 29,554 | 30,415 | 32,336 | 35,747 | 34,705 |
| Total | $722,921 | $756,289 | $878,844 | $917,461 | $926,135 |

(p) Preliminary

(1) Estimated

(2) Amounts of federal grants to the Health Facilities and Services Administration, which is a public corporation, are not included in the Health Area. For fiscal years 1992, 1993 and 1994, the federal funds to this agency total $262.4, $274.8 and $274.8 million, respectively.

(3) Funds approved for the Job Training Partnership Act Program and Community Service Block Grant previously administered by the Office of Economic Opportunity were transferred in fiscal year 1989 to the Right to Work Administration, the Council on Technology Formation and the Child Services and Community Development Office. The total amounts of federal grants to these agencies are not included in these figures.

(4) Amounts presented in this area do not include grants to the Public Housing Administration and Urban Renewal and Housing Corporation.

(5) Amount includes funds approved by FEMA for the construction of permanent housing to the affected families who lost their homes due to Hurricane Hugo damages.

(6) Amount includes Section 8 Housing Assistance Funds which are transferred to the Department of Housing due to the Urban Renewal Housing Corporation's dissolution in fiscal year 1992

(7) Includes disaster relief funds authorized by FEMA to the Commonwealth for Public Assistance Program and state administrative expenses for the operation of the Individual and Family Grant activities. Funds going directly to individuals to meet those disaster related needs are not considered in these figures. For fiscal years 1990 and 1991, amounts include funds received due to Hurricane Hugo which occurred in September 1989. The amount in 1992 represents an estimate of funds approved by FEMA due to the flooding of January 1992.

*Source:* Office of Budget and Management

## COMMONWEALTH BUDGET

### Office of Budget and Management

The fundamental objective of the Office of Budget and Management ("OBM") is to improve and strengthen the relationship between policy formulation and budgetary and fiscal management. The law creating OBM also strengthened budgetary controls and created an Operational Audit Division with the primary function of evaluating government operations and programs.

The annual budget includes the public corporations as well as the Commonwealth government; however, the following describes only the Commonwealth budget.

### Budgetary Process

The fiscal year of the Commonwealth begins on July 1. The Governor is constitutionally required to submit to the Legislature an annual budget of capital improvements and operating expenses of the Commonwealth for the ensuing fiscal year. The annual budget is prepared by OBM, working with the Planning Board, the Department of the Treasury, and other government offices and agencies. Section 7 of Article VI of the Constitution provides that "The appropriations made for any fiscal year shall not exceed the total revenues, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law."

The annual budget, which is developed utilizing elements of program budgeting and zero-base budgeting, includes an estimate of revenues and other resources for the ensuing fiscal year under (i) laws existing at the time the budget is submitted and (ii) legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor's recommendations as to appropriations that in his judgment are necessary, convenient, and in conformity with the four-year investment plan prepared by the Planning Board.

The Legislature may amend the budget submitted by the Governor but may not increase any items so as to cause a deficit without imposing taxes to cover such deficit. Upon passage by the Legislature, the budget is referred to the Governor who may decrease or eliminate any item but may not increase or insert any new item in the budget. The Governor may also veto the budget in its entirety and return it to the Legislature with his objections. The Legislature, by a two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the end of the fiscal year, the annual budget for the preceding fiscal year as originally approved by the Legislature and the Governor is automatically renewed for the ensuing fiscal year until a new budget is approved by the Legislature and the Governor. This permits the Commonwealth to continue to make payments of its operating and other expenses until a new budget is approved.

### Financial Control and Adjustment Procedures

Revenue estimates for budgetary purposes are prepared by the Department of the Treasury, except for estimates of federal grants, which are prepared by OBM and various departments and other recipients of such grants. Revenue and federal grant estimates are under continuous review and, if necessary, are revised at least quarterly during the fiscal year. Fiscal control over expenditures is exercised severally by the Governor, through the Director of OBM, and the Secretary of the Treasury. Quarterly reviews and expenditure cut-off procedures are designed to prevent expenditures in excess of appropriations.

During any fiscal year in which the resources available to the Commonwealth are insufficient to cover the appropriations approved for such year, the Governor may take administrative measures to reduce expenses and submit to both houses of the Legislature a detailed report of any adjustment necessary to balance the budget, or make recommendations to the Legislature for new taxes, or take any other necessary action to meet the estimated deficiency, or authorize borrowings under provisions of existing legislation. Any such proposed adjustments shall give effect to the "priority norms" established by law for the disbursement of public funds in the following order of priority: first, the payment of the interest on and amortization requirements for public debt (Commonwealth general obligations and guaranteed debt for which the Commonwealth's guarantee has been exercised); second, the fulfillment of obligations arising out of legally binding contracts, court decisions on eminent domain and certain commitments to protect the name, credit and good faith of the Commonwealth government; third, current expenditures in the areas of health, protection of persons and property, education, welfare and retirement systems; and fourth, all other purposes.

A Budgetary Fund was created by Act No. 147, approved by the Legislature of Puerto Rico on June 18, 1980. The Budgetary Fund is used to cover the appropriations approved in any fiscal year in which the revenues available for such fiscal year are insufficient, to honor the public debt and to provide for unforeseen circumstances in the provision of public services. The Secretary of the Treasury may transfer up to $7 million to the Budgetary Fund from unencumbered surpluses at the end of each fiscal year. The Governor may transfer an amount greater than $7 million to the Budgetary Fund so long as the maximum balance does not exceed 3% of the funds appropriated in the budget joint resolution for the fiscal year in which such funds are to be covered into the Budgetary Fund.

**Appropriations**

Appropriations in the Central Government Budget of the Commonwealth consist of the following:

(i) General Fund appropriations for recurring ordinary operating expenses of the Central Government and for contributions to public corporations, municipalities, and private organizations. Such appropriations are made by a single annual law known as the Joint Resolution of the General Budget.

(ii) General Fund appropriations for special operating expenses and for capital expenditures. Such appropriations are authorized by separate laws for one or more years for special programs or activities, which may be permanent or transitory.

(iii) Disbursements of Special Funds for operating purposes and for capital improvements. For the most part, such disbursements do not require annual legislative authorization, because they are authorized by previous legislation or by the United States Congress. Federal grants constitute the major part of the resources of the Special Funds.

(iv) Bond Fund appropriations for capital expenditures financed by bonds. Such expenditures may occur in one or more years.

In Puerto Rico, the Central Government has many functions which in the 50 states are the responsibility of local government, such as providing public education and police and fire protection. The central government also makes large annual grants to the University of Puerto Rico and to the municipalities, including reimbursement for property taxes which they do not collect because of the property tax exemption on the first $15,000 of assessed valuation of owner-occupied residences. See "Major Sources of General Fund Revenues — Property Taxes" under *Commonwealth Taxes, Other Revenues and Expenditures.* In the summaries of the budgets of the Central Government presented below, grants to the University of Puerto Rico are included in current expenses for education and debt service on general obligation bonds is included in current expenses for debt service. Debt service on Sugar Corporation notes paid by the Commonwealth is included in current expenses for economic development, and debt service on Urban Renewal and Housing Corporation bonds and notes and on Housing Bank and Finance Agency mortgage subsidy bonds paid by the Commonwealth is included in current expenses for housing.

Approximately 24.6% of the Central Government Budget is committed, including debt service on direct debt of the Commonwealth and on the debt of the Sugar Corporation, municipal subsidies, grants to the University of Puerto Rico, and rental payments to Public Buildings Authority, among others.

### Fiscal 1993 Budget

The following table presents a summary of the Commonwealth budget for the fiscal year ending June 30, 1993.

**Commonwealth of Puerto Rico**
**Central Government Annual Budget**
**Fiscal Year Ending June 30, 1993**
**(in thousands)**

| | General Fund | Bond Fund | Special Funds | Total |
|---|---|---|---|---|
| Resources: | | | | |
| Revenues from internal sources: | | | | |
| Property taxes | $ 0 | $ — | $ 62,080 | $ 62,080 |
| Personal income taxes | 1,235,000 | — | — | 1,235,000 |
| Retained non-resident income taxes | 52,000 | — | — | 52,000 |
| Corporation income taxes | 976,000 | — | — | 976,000 |
| Partnership income taxes | 1,000 | — | — | 1,000 |
| Tollgate taxes | 120,000 | — | — | 120,000 |
| Interest subject to 17% | 6,000 | — | — | 6,000 |
| Dividends subject to 20% | 28,000 | — | — | 28,000 |
| Inheritance and gift taxes | 1,000 | — | — | 1,000 |
| Excise taxes: | | | | |
| Alcoholic beverages | 214,000 | — | — | 214,000 |
| Motor vehicles and accessories | 200,000 | — | 200 | 200,200 |
| Cigarettes | 104,000 | — | — | 104,000 |
| Special excise tax on certain petroleum products | 120,000 | — | — | 120,000 |
| Other | 389,000 | — | 77,172 | 466,172 |
| Licenses | 48,000 | — | — | 48,000 |
| Miscellaneous non-tax revenues: | | | | |
| Contributions from lottery fund | 63,000 | — | — | 63,000 |
| Electronic lottery | 54,000 | — | — | 54,000 |
| Registration and document certification fees | 64,000 | — | — | 64,000 |
| Other | 40,000 | — | 111,595 | 151,595 |
| Total revenues from internal sources | 3,715,000 | — | 251,047 | 3,966,047 |
| Revenues from non-Commonwealth sources: | | | | |
| Federal excise taxes on off-shore shipments | 180,000 | — | 14,500 | 194,500 |
| Federal grants | — | — | 917,460(a) | 917,460 |
| Customs | 95,000 | — | 0 | 95,000 |
| Total revenues from non-Commonwealth sources | 275,000 | — | 931,960 | 1,206,960 |
| Total revenues | 3,990,000 | — | 1,183,007 | 5,173,007 |
| Other: | | | | |
| Other income from: | | | | |
| Investment interest | 14,000 | — | — | 14,000 |
| Surplus from prior year appropriations and encumbrances | 39,759 | — | — | 39,759 |
| Reimbursement of excess reserves from PBA | 15,012 | — | — | 15,012 |
| Miscellaneous income | 8,285 | — | — | 8,285 |
| Total other income | 77,056 | — | — | 77,056 |
| TLD sale | 95,618 | — | — | 95,618 |
| Savings from Refunding Bonds | 11,400 | — | — | 11,400 |
| Balance from previous year | 31,073 | — | 330,914 | 361,987 |
| Bonds authorized | — | 310,000 | — | 310,000 |
| Total other sources | 215,147 | 310,000 | 330,914 | 856,061 |
| Total resources | $4,205,147 | $310,000 | $1,513,921 | $6,029,068 |
| Appropriations: | | | | |
| Current expenses: | | | | |
| Appropriations controlled by the Office of Budget and Management | $ 0 | $ — | — | $ 0 |
| Reserve to reimburse the General Fund | 30,000 | — | — | 30,000 |
| General government | 285,599 | — | 8,484 | 294,083 |
| Education | 1,392,050 | — | 476,353 | 1,868,403 |
| Health | 532,198 | — | 65,826 | 598,024 |
| Welfare | 300,451 | — | 356,502 | 656,953 |
| Economic development | 320,024 | — | 39,651 | 359,675 |
| Public safety and protection | 636,109 | — | 42,543 | 678,652 |
| Transportation and communications | 86,804 | — | 4,481 | 91,285 |
| Housing | 92,332 | — | 3,054 | 95,386 |
| Contributions to municipalities | 211,209 | — | 1,647 | 212,856 |
| Special pension contributions | 16,962 | — | 0 | 16,962 |
| Debt service | 296,891 | — | 62,080 | 358,971 |
| Total appropriations — current expenses | 4,200,629 | — | 1,060,621 | 5,261,250 |
| Capital improvements | 4,518 | 310,000 | 61,049 | 375,567 |
| Total appropriations | 4,205,147 | 310,000 | 1,121,670 | 5,636,817 |
| Year-end balance | 0 | — | 392,251 | 392,251 |
| Total appropriations and year-end balance | $4,205,147 | $310,000 | $1,513,921 | $6,029,068 |

(a) Does not include grants received by the Administration of Health Services and Facilities nor those of other agencies whose accounting systems are not centralized in the Department of the Treasury.

*Sources:* Department of the Treasury resources and Office of Budget and Management appropriations, as reported on April 14, 1993

In the fiscal 1993 budget, revenues and other resources of all budgetary funds total $5,357,081,000, excluding balances from the previous fiscal year and general obligation bonds authorized. The estimated increases in General Fund revenues in fiscal 1993 are accounted for by increases in personal income taxes (up $112,665,000), tollgate taxes (up $21,498,000), other excise taxes and registration fees (up $48,671,000). These increases are offset by a decrease in other sources (down $178,231,000 attributable to a decrease in non-recurring revenues); corporation income taxes (down $43,468,000); and property taxes (down $15,003,000 due to the transfer from the General Fund to Municipalities pursuant to Act No. 80).

Current expenses and capital improvements, other than those financed by bonds, of all budgetary funds total $5,326,817,000, an increase of $113,702,000 over fiscal 1992. The major changes in General Fund expenditures by program in fiscal 1993 are: education (up $120,620,000), public safety and protection (up $38,811,000), debt service (up $12,327,000), welfare (up $7,188,000), general government (down $80,086,000), appropriations controlled by the Office of Budget and Management (down $69,033,000), economic development (down $32,281,000), and housing (down $20,333,000).

The general obligation bond authorization approved for the fiscal 1993 budget is $310,000,000.

## Fiscal 1994 Budget

The following table presents a summary of the Commonwealth budget for the fiscal year ending June 30, 1994.

**Commonwealth of Puerto Rico**
**Central Government Annual Budget**
**Fiscal Year Ending June 30, 1994**
**(in thousands)**

| | General Fund | Bond Fund | Special Funds | Total |
|---|---|---|---|---|
| Resources | | | | |
| Revenues from internal sources: | | | | |
| Property taxes | $ 0 | $ — | $ 63,140 | $ 63,140 |
| Personal income taxes | 1,356,000 | — | — | 1,356,000 |
| Retained non-resident income taxes | 49,000 | — | — | 49,000 |
| Corporation income taxes | 1,066,000 | — | — | 1,066,000 |
| Partnership income taxes | 1,000 | — | — | 1,000 |
| Tollgate taxes | 160,000 | — | — | 160,000 |
| Interest subject to 17% | 6,000 | — | — | 6,000 |
| Dividends subject to 20% | 30,000 | — | — | 30,000 |
| Inheritance and gift taxes | 1,000 | — | — | 1,000 |
| Excise taxes: | | | | |
| Alcoholic beverages | 216,000 | — | — | 216,000 |
| Motor vehicles and accessories | 200,000 | — | 200 | 200,200 |
| Cigarettes | 104,000 | — | — | 104,000 |
| Special excise tax on certain petroleum products | 120,000 | — | — | 120,000 |
| Other | 406,000 | — | 80,324 | 486,324 |
| Licenses | 50,000 | — | — | 50,000 |
| Miscellaneous non-tax revenues: | | | | |
| Contributions from lottery fund | 62,000 | — | — | 62,000 |
| Electronic lottery | 54,000 | — | — | 54,000 |
| Registration and document certification fees | 62,000 | — | — | 62,000 |
| Other | 42,000 | — | 117,236 | 159,236 |
| Total revenues from internal sources | 3,985,000 | — | 260,900 | 4,245,900 |
| Revenues from non-Commonwealth sources: | | | | |
| Federal excise taxes on off-shore shipments | 180,000 | — | 14,500 | 194,500 |
| Federal grants | — | — | 926,133(1) | 926,133 |
| Customs | 95,000 | — | 0 | 95,000 |
| Total revenues from non-Commonwealth sources | 275,000 | — | 940,633 | 1,215,633 |
| Total revenues | 4,260,000 | — | 1,201,533 | 5,461,533 |
| Other: | | | | |
| Other income from: | | | | |
| Investment interest | 11,725 | — | — | 11,725 |
| Surplus from prior year appropriations and encumbrances | 22,000 | — | — | 22,000 |
| Reimbursement of excess reserves from PBA | 28,000(2) | — | — | 28,000 |
| Miscellaneous income | 18,000(3) | — | — | 18,000 |
| Total, other income | 79,725 | — | — | 79,725 |
| Savings from Refunding Bonds | 13,000 | — | — | 13,000 |
| Balance from previous year | 0 | — | 392,252 | 392,252 |
| Bonds authorized | — | 300,000 | — | 300,000 |
| Total other sources | 92,725 | 300,000 | 392,252 | 784,977 |
| Total resources | $4,352,725 | $300,000 | $1,593,785 | $6,246,510 |
| Appropriations: | | | | |
| Current expenses: | | | | |
| Appropriations controlled by the Office of Budget and Management | $ 0 | $ — | $ — | $ 0 |
| Reserve to reimburse the General Fund | 30,000 | — | — | 30,000 |
| General Government | 271,029 | — | 3,205 | 274,234 |
| Education | 1,341,627 | — | 492,320 | 1,833,947 |
| Health | 647,308 | — | 87,181 | 734,489 |
| Welfare | 262,284 | — | 328,231 | 590,515 |
| Economic development | 328,540 | — | 39,620 | 368,160 |
| Public safety and protection | 745,369 | — | 41,877 | 787,246 |
| Transportation and communications | 88,390 | — | 6,902 | 95,292 |
| Housing | 89,970 | — | 1,795 | 91,765 |
| Contributions to municipalities | 230,371 | — | 1,657 | 232,028 |
| Special pension contributions | 17,837 | — | 0 | 17,837 |
| Debt service | 300,000 | — | 63,140 | 363,140 |
| Total appropriations — current expenses | 4,352,725 | — | 1,065,928 | 5,418,653 |
| Capital improvements | 0 | 300,000 | 63,890 | 363,890 |
| Total appropriations | 4,352,725 | 300,000 | 1,129,818 | 5,782,543 |
| Year-end balance | 0 | — | 463,967 | 463,967 |
| Total appropriations and year-end balance | $4,352,725 | $300,000 | $1,593,785 | $6,246,510 |

(1) Does not include grants received by the Administration of Health Services and Facilities nor those of other agencies whose accounting systems are not centralized in the Department of the Treasury

(2) Represents rent payment adjustment as a result of previous Public Buildings Authority bond refundings.

(3) Includes $12,000,000 from "payment in lieu of taxes" to be made by the Telephone Authority.

*Sources:* Department of the Treasury resources and Office of Budget and Management appropriations, as reported on April 14, 1993

In the fiscal 1994 budget, revenues and other resources of all budgetary funds total $5,554,258,000, excluding balances from the previous fiscal year and general obligation bonds authorized. The estimated increases in General Fund revenues in fiscal 1994 are accounted for by increases in personal income taxes (up $121,000,000), corporation income taxes (up $90,000,000), tollgate taxes (up $40,000,000), and other excise taxes (up $17,000,000). These increases are offset by decreases in other revenues (down $122,422,000) reflecting the non-recurring nature of the fiscal 1993 sale of TLD.

Current expenses and capital improvements, other than those financed by bonds, of all budgetary funds total $5,482,543,000, an increase of $155,726,000 from fiscal 1993. The major changes in General Fund expenditures by program in fiscal 1994 are: health (up $115,110,000), public safety and protection (up $109,260,000), contributions to municipalities (up $19,162,000), economic development (up $8,516,000), debt service (up $3,109,000), education (down $50,423,000), welfare (down $38,167,000), general government (down $14,570,000), and housing (down $2,362,000).

Approximately $98,395,295 of budgetary expenditures in fiscal 1994 represent salary increases included within the applicable program areas of the budget.

The proposed general obligation bond authorization for the fiscal 1994 budget is $300,000,000.

**Differences between Budget and General Purpose Financial Statements**

Revenues and expenditures, as reported by the Department of the Treasury in its General Purpose Financial Statements, may differ substantially from resources and appropriations in the annual budget for a number of reasons, including the following:

(i) The budgetary accounts are on a cash basis, while the financial statements prepared by the Department of the Treasury include accruals and other adjustments as required by government accounting standards.

(ii) Expenditures for current purposes in a particular fiscal year may include amounts appropriated for earlier periods but not previously expended and, conversely, may exclude amounts appropriated for such fiscal year but not expended until later periods.

(iii) Bonds are authorized by the Commonwealth in accordance with a four-year capital improvement program. Since bond sales are determined by bond market conditions and other factors, the amount of bonds sold in any year does not necessarily equal the amount of bonds authorized in the budget for that year. Expenditures for capital improvements are financed by advances from the General Fund to the Capital Projects Fund, which are later reimbursed from proceeds of bond or note sales.

(iv) Advances are made from the General Fund to municipalities and to public corporations and other entities, pending reimbursement from later collections of municipal property taxes and other sources.

KPMG Peat Marwick

APPENDIX II

# COMMONWEALTH OF PUERTO RICO

General Purpose Financial Statements

June 30, 1991

COMMONWEALTH OF PUERTO RICO

General Purpose Financial Statements

June 30, 1991

## Table of Contents

KPMG Peat Marwick

Certified Public Accountants

PO Box 364089
San Juan PR 00936-4089

## Independent Auditors' Report

The Governor of the
Commonwealth of Puerto Rico:

We have audited the general purpose financial statements of the Commonwealth of Puerto Rico as of and for the year ended June 30, 1991 as listed in the accompanying table of contents. These general purpose financial statements are the responsibility of the management of the Commonwealth. Our responsibility is to express an opinion on these general purpose financial statements based on our audit. We did not audit the financial statements of certain component units, which represent the indicated percent of total assets and total revenues, respectively, of the Special Revenue Fund (6% and 6%), Debt Service Fund (10% and 2%), Enterprise Fund (41% and 36%) and Internal Service Fund (99% and 95%), and the General Long-term Debt Account Group (9% of total debt). Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for those component units, is based solely on the reports of the other auditors, which include certain reports that were qualified as described in note 16 to the general purpose financial statements.

Except as discussed in the following three paragraphs, we conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the general purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinion.

We did not, nor did other auditors, audit the financial statements of certain component units, which reflect total assets and revenues constituting 44% and 1%, of the Special Revenue Fund and 13% and 6% of the Enterprise Fund, respectively, of total assets and revenues of each of these funds.

As discussed in note 4 to the general purpose financial statements, the balance of loans receivable from participants, including related accrued interest receivable, and escrow liability of the Annuity and Pension System for the Teachers of Puerto Rico, the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities and of the Puerto Rico Judiciary Retirement System is based on estimates as the actual amounts cannot be determined. Accordingly, we were unable to satisfy ourselves as to the balance of loans receivable from participants, escrow liability and the related investment earnings which are presented in the Fiduciary Funds.

As discussed in note 5 to the general purpose financial statements, the Commonwealth has not maintained complete records relating to certain general fixed assets. Accordingly, we were unable to satisfy ourselves as to the balance of general fixed assets.

As described in note 12, the general purpose financial statements do not include a combined statement of revenues and expenditures - budget and actual - general fund which should be included to conform with generally accepted accounting principles.

As described in notes 14 and 15 to the general purpose financial statements, the Commonwealth accounts for certain pension costs on a basis other than the basis of accounting required by generally accepted accounting principles. This departure from generally accepted accounting principles has resulted in the Public University Funds not providing $144 million of pension costs through June 30, 1991. The effect of the departure on the governmental funds and general long-term debt account group has not been determined as the required actuarial computations have not been prepared.

As described in note 16 to the general purpose financial statements, the Puerto Rico Urban Renewal and Housing Corporation included in the Enterprise Fund did not provide depreciation on fixed assets. Also, an undetermined amount of such fixed assets is available for sale but their net realizable value cannot be presently determined. Such fixed assets should have been depreciated over their estimated useful lives and the carrying value of fixed assets available for sale should have been reduced to net realizable value, if lower, to conform with generally accepted accounting principles. The effect on the general purpose financial statements of the lack of depreciation and the reduction to net realizable value is not reasonably determinable.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to audit the financial statements of certain unaudited component units and examine adequate records to support the balance of loans receivable from participants, escrow liability, related investment earnings and general fixed assets as discussed in the third, fourth and fifth paragraphs and except for the effects on the general purpose financial statements of the omission described in the sixth paragraph and of not accounting for pension costs, depreciation and realization of fixed assets available for sale as required by generally accepted accounting principles as described in the seventh and eighth paragraphs, based on our audit and the reports of other auditors, the general purpose financial statements referred to above presents fairly, in all material respects, the financial position of the Commonwealth of Puerto Rico as of June 30, 1991, the results of its operations and cash flows of its proprietary fund types for the year then ended in conformity with generally accepted accounting principles.

As discussed in note 1E to the general purpose financial statements, the Commonwealth of Puerto Rico adopted Statement No. 9 of the Governmental Accounting Standards Board which requires the presentation of a statement of cash flows and certain other disclosures.

KPMG Peat Marwick

April 10, 1992, except for note 18 as to which the date is June 4, 1992

Stamp No. 1074630 of the Puerto Rico Society of Certified Public Accountants was affixed to the record copy of this report.

COMMONWEALTH OF PUERTO RICO

Combined Balance Sheet - All Fund Types and Account Groups

June 30, 1991
(In thousands)

| Assets and Other Debits | Governmental Fund Types: General | Governmental Fund Types: Special Revenue | Governmental Fund Types: Debt Service | Governmental Fund Types: Capital Projects | Proprietary Fund Types: Enterprise | Proprietary Fund Types: Internal Service | Fiduciary Fund Types: Trust and Agency | Account Groups: General Fixed Assets (Unaudited) | Account Groups: General Long-term Debt | Public University Funds | Totals (Memorandum Only) |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Cash, cash equivalents and investments (note 2) | $ - | 68,983 | 264,035 | 2,552 | 757,067 | 3,279,680 | 2,310,544 | - | - | 30,753 | 6,713,614 |
| Cash, cash equivalents and investments in governmental banks (note 3) | 150,368 | 80,820 | 229,324 | 297,422 | 1,275,252 | 88,277 | 482,133 | - | - | - | 2,603,596 |
| Receivables, net (note 4): | | | | | | | | | | | |
| Taxes | 79,217 | - | 1,990 | - | - | - | 76,593 | - | - | - | 157,800 |
| Federal Government | - | 50,234 | - | 34,303 | 19,906 | - | 2,213 | - | - | - | 106,656 |
| Accounts | - | 41,661 | - | - | 810,908 | 28,454 | 33,065 | - | - | - | 914,088 |
| Loans and advances | 25,514 | 26,409 | - | - | 194,617 | 1,607,566 | 518,601 | - | - | 3,072 | 2,375,779 |
| Accrued interest | 8,613 | 3,329 | 8,994 | 563 | 30,058 | 90,820 | 14,630 | - | - | - | 157,007 |
| Other | - | 1,561 | - | - | 38,468 | 22,892 | - | - | - | 3,623 | 66,544 |
| Due from other funds (notes 7 and 11) | 156,694 | 80,038 | 34,767 | 10,081 | 189,195 | 35,080 | 40,948 | - | - | 5,315 | 552,118 |
| Inventories | - | - | - | - | 322,547 | 160,890 | - | - | - | 4,929 | 488,366 |
| Restricted assets (notes 2, 3, 7, 15 and 16) | 595,946 | 42,746 | - | - | 1,446,130 | 2,028,459 | - | - | - | 61,494 | 4,174,775 |
| Fixed assets, net (notes 5, 15 and 16) | - | - | - | - | 8,750,252 | 939,883 | 67,881 | 2,264,246 | - | 397,364 | 12,419,626 |
| Other assets | - | 1,137 | - | 228 | 493,786 | 76,054 | 748 | - | - | 508 | 572,461 |
| Amount available in debt service fund | - | - | - | - | - | - | - | - | 195,098 | - | 195,098 |
| Amount to be provided for retirement of bonds and notes payable | - | - | - | - | - | - | - | - | 4,611,582 | - | 4,611,582 |
| Amount to be provided for payment of due to other funds, accrued compensated absences, and other long-term liabilities | - | - | - | - | - | - | - | - | 834,678 | - | 834,678 |
| Total assets and other debits | $ 1,016,352 | 396,918 | 539,110 | 345,149 | 14,328,186 | 8,358,055 | 3,547,356 | 2,264,246 | 5,641,358 | 507,058 | 36,943,788 |

COMMONWEALTH OF PUERTO RICO

Combined Balance Sheet - All Fund Types and Account Groups

June 30, 1991
(In thousands)

| | Governmental Fund Types | | | | Proprietary Fund Types | | Fiduciary Fund Types | Account Groups | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Liabilities | General | Special Revenue | Debt Service | Capital Projects | Enterprise | Internal Service | Trust and Agency | General Fixed Assets (Unaudited) | General Long-term Debt | Public University Funds | Totals (Memorandum Only) |
| Accounts payable and accrued liabilities | $ 224,466 | 209,171 | 5,083 | 75,293 | 1,858,891 | 134,805 | 35,144 | - | - | 43,341 | 2,586,194 |
| Tax refunds payable | 93,410 | - | - | - | - | - | - | - | - | - | 93,410 |
| Deposits (notes 3 and 16) | - | - | - | - | 427,212 | 4,282,464 | - | - | - | - | 4,709,676 |
| Due to other funds (notes 7 and 11) | 62,582 | 122,864 | - | 35,086 | 16,490 | 59,934 | 98,453 | - | 129,988 | - | 525,397 |
| Securities sold under agreements to repurchase | - | - | - | - | 121,502 | 468,337 | - | - | - | - | 589,839 |
| Interest payable | 11,100 | 13,108 | 143,289 | - | 211,746 | 106,917 | - | - | - | - | 486,160 |
| Deferred revenue | 13,283 | 29,310 | - | - | 33,603 | - | 17,508 | - | - | - | 93,704 |
| Notes payable (notes 6, 7, 15 and 16) | 483,596 | 40,984 | - | - | 2,211,438 | 325,088 | - | - | 350,000 | 8,263 | 3,419,369 |
| Bonds payable (notes 7, 15 and 16) | - | - | 195,640 | - | 4,940,461 | 2,073,664 | - | - | 2,982,491 | 191,319 | 10,383,575 |
| Appropriation and revenue bonds and notes payable of component units (note 8) | - | - | - | - | - | - | - | - | 1,474,189 | - | 1,474,189 |
| Accrued compensated absences | - | - | - | - | 259,783 | 15,953 | 2,495 | - | 453,800 | 19,562 | 751,593 |
| Other liabilities (note 4) | 14,153 | 789 | - | 2,148 | - | - | 687,163 | - | - | - | 704,253 |
| Other long-term liabilities (notes 10 and 13) | - | - | - | - | 86,673 | 1,389 | - | - | 250,890 | - | 338,952 |
| Total liabilities | 902,590 | 416,226 | 344,012 | 112,527 | 10,167,799 | 7,468,551 | 840,763 | - | 5,641,358 | 262,485 | 26,156,311 |
| **Fund Equity/(Deficit) and Other Credits** | | | | | | | | | | | |
| Contributed capital (note 16) | - | - | - | - | 4,425,354 | 783,265 | - | - | - | - | 5,208,619 |
| Investment in general fixed assets | - | - | - | - | - | - | - | 2,264,246 | - | 206,465 | 2,470,711 |
| Retained earnings/(deficit) | - | - | - | - | (264,967) | 106,239 | - | - | - | - | (158,728) |
| Fund balance/(deficit): | | | | | | | | | | | |
| Reserved for: | | | | | | | | | | | |
| Encumbrances | 61,170 | 2,119 | - | 5,068 | - | - | 3,354 | - | - | 23,025 | 94,736 |
| Debt service (note 8) | - | - | 195,098 | - | - | - | - | - | - | 21,565 | 216,663 |
| Employees' retirement | - | - | - | - | - | - | 1,779,389 | - | - | - | 1,779,389 |
| Unemployment benefits | - | - | - | - | - | - | 780,282 | - | - | - | 780,282 |
| Other specified purposes | 144,248 | 1,485 | - | 174,656 | - | - | 143,568 | - | - | 9,564 | 473,521 |
| Unreserved | (91,656) | (22,912) | - | 52,898 | - | - | - | - | - | (16,046) | (77,716) |
| Total fund equity/(deficit) and other credits | 113,762 | (19,308) | 195,098 | 232,622 | 4,160,387 | 889,504 | 2,706,593 | 2,264,246 | - | 244,573 | 10,787,477 |
| Commitments and contingencies (notes 9, 10, 13, 15 and 16) | | | | | | | | | | | |
| Total liabilities, fund equity/(deficit) and other credits | $ 1,016,352 | 396,918 | 539,110 | 345,149 | 14,328,186 | 8,358,055 | 3,547,356 | 2,264,246 | 5,641,358 | 507,058 | 36,943,788 |

See accompanying notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

Combined Statement of Revenues, Expenditures and Changes in Fund Balance/(Deficit) - All Governmental Fund Types and Expendable Trust Funds

Year ended June 30, 1991
(In thousands)

| | Governmental Fund Types | | | | Fiduciary Fund Types | |
|---|---|---|---|---|---|---|
| | General | Special Revenue | Debt Service | Capital Projects | Expendable Trust | Totals (Memorandum Only) |
| Revenues: | | | | | | |
| Taxes (notes 4 and 8): | | | | | | |
| Income | $ 2,318,144 | - | - | - | - | 2,318,144 |
| Property | 127,635 | - | 67,380 | - | - | 195,015 |
| Excise, including reimbursement of Federal excise taxes of $215,003 | 1,153,717 | - | 129,553 | - | - | 1,283,270 |
| Other | 39,962 | 6,805 | 689 | - | 222,739 | 270,195 |
| Charges for services | 546,941 | 3,346 | - | - | 2,265 | 552,552 |
| Intergovernmental | 104,575 | 1,935,610 | - | 74,399 | 55,681 | 2,170,265 |
| Other | 115,743 | 12,662 | 86,883 | 2,974 | 65,373 | 283,635 |
| Total revenues | 4,406,717 | 1,958,423 | 284,505 | 77,373 | 346,058 | 7,073,076 |
| Expenditures: | | | | | | |
| Current: | | | | | | |
| General government | 452,769 | 1,058 | - | - | - | 453,827 |
| Public safety | 548,020 | 25,423 | - | - | 88 | 573,531 |
| Health | 111,156 | 92,874 | - | - | - | 204,030 |
| Public housing and welfare | 235,074 | 1,082,807 | - | - | 52,936 | 1,370,817 |
| Education | 838,112 | 457,108 | - | - | - | 1,295,220 |
| Economic development | 176,688 | 348,476 | - | - | 200,191 | 725,355 |
| Aid to municipalities (note 4) | 327,245 | 45,403 | - | - | - | 372,648 |
| Lottery prizes | 314,866 | - | - | - | - | 314,866 |
| Capital outlays | 75,160 | 10,382 | - | 566,197 | 9,399 | 661,138 |
| Debt service: | | | | | | |
| Principal | 33,915 | - | 492,315 | - | - | 526,230 |
| Interest and other | 24,571 | - | 333,975 | - | - | 358,546 |
| Total expenditures | 3,137,576 | 2,063,531 | 826,290 | 566,197 | 262,614 | 6,856,208 |
| Excess/(deficiency) of revenues over/(under) expenditures | 1,269,141 | (105,108) | (541,785) | (488,824) | 83,444 | 216,868 |
| Other financing sources/(uses): | | | | | | |
| Proceeds from long-term debt issues (note 7) | - | - | 513,592 | 426,502 | - | 940,094 |
| Operating transfers in (note 11) | 6,616 | 152,560 | 400,515 | 145,176 | 7,100 | 711,967 |
| Other sources | 78,106 | 1,495 | - | 22,010 | 2,272 | 103,883 |
| Operating transfers out (note 11) | (1,419,900) | (44,332) | (110,227) | (73,254) | (11) | (1,647,724) |
| Payment of refunded bonds | - | - | (261,293) | - | - | (261,293) |
| Other uses | (40,235) | (6,135) | (804) | (274) | (1,530) | (48,978) |
| Total other financing sources/(uses), net | (1,375,413) | 103,588 | 541,783 | 520,160 | 7,831 | (202,051) |
| Excess/(deficiency) of revenues and other financing sources over/(under) expenditures and other financing uses | (106,272) | (1,520) | (2) | 31,336 | 91,275 | 14,817 |
| Fund balance/(deficit) at beginning of year | 260,618 | (18,976) | 195,100 | 201,286 | 835,929 | 1,473,957 |
| Residual equity transfers out (note 11) | (40,584) | - | - | - | - | (40,584) |
| Effect of inclusion of prior year operations (note 1(U)) | - | 1,188 | - | - | - | 1,188 |
| Fund balance/(deficit) at end of year | $ 113,762 | (19,308) | 195,098 | 232,622 | 927,204 | 1,449,378 |

See accompanying notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

Combined Statement of Revenues, Expenses and Changes
in Retained Earnings/(Deficit)/Fund Balance - All
Proprietary Fund Types and Pension Trust Funds

Year ended June 30, 1991
(In thousands)

| | Proprietary Fund Types | | Fiduciary Fund Types | |
|---|---|---|---|---|
| | Enterprise | Internal Service | Pension Trust | Totals (Memorandum Only) |
| Operating revenues: | | | | |
| Charges for services | $ 3,463,616 | 228,492 | - | 3,692,108 |
| Financing income | 20,059 | 135,785 | - | 155,844 |
| Investment earnings | 93,139 | 351,279 | 173,720 | 618,138 |
| Contributions to retirement systems | - | - | 386,336 | 386,336 |
| Other | 86,619 | 3,542 | - | 90,161 |
| Total operating revenues | 3,663,433 | 719,098 | 560,056 | 4,942,587 |
| Operating expenses: | | | | |
| Cost of services | 3,668,420 | 139,590 | 32,507 | 3,840,517 |
| Retirement benefits | - | - | 371,136 | 371,136 |
| Interest | 112,985 | 454,223 | - | 567,208 |
| Depreciation and amortization | 370,194 | 30,917 | - | 401,111 |
| Other | 8,104 | 14,919 | - | 23,023 |
| Total operating expenses | 4,159,703 | 639,649 | 403,643 | 5,202,995 |
| Operating income/(loss) | (496,270) | 79,449 | 156,413 | (260,408) |
| Non-operating revenues/(expenses): | | | | |
| Federal subsidies and grants | 145,505 | - | - | 145,505 |
| Interest income | 166,339 | 25,036 | - | 191,375 |
| Interest expense | (336,706) | (23) | - | (336,729) |
| Other, net | (99,781) | 1,816 | - | (97,965) |
| Total non-operating revenues/(expenses), net | (124,643) | 26,829 | - | (97,814) |
| Income/(loss) before operating transfers and extraordinary gain | (620,913) | 106,278 | 156,413 | (358,222) |
| Operating transfers in | 608,394 | 3,000 | - | 611,394 |
| Operating transfers out | (41,704) | - | - | (41,704) |
| Operating transfers, net (note 11) | 566,690 | 3,000 | - | 569,690 |
| Income/(loss) before extraordinary gain | (54,223) | 109,278 | 156,413 | 211,468 |
| Extraordinary gain (note 16) | 14,418 | - | - | 14,418 |
| Net income/(loss) | (39,805) | 109,278 | 156,413 | 225,886 |
| Retained earnings/(deficit)/fund balance at beginning of year: | | | | |
| As previously reported | (164,124) | 86,377 | 1,690,108 | 1,612,361 |
| Restatements (notes 4 and 17) | (13,016) | - | (67,132) | (80,148) |
| As restated | (177,140) | 86,377 | 1,622,976 | 1,532,213 |
| Contributions | 32,784 | - | - | 32,784 |
| Transfers from/(to) contributed capital | 22,997 | (130,000) | - | (107,003) |
| Residual equity transfers in/(out) (note 11) | (76,000) | 40,584 | - | (35,416) |
| Effect of inclusion of prior year operations (note 1(U)) | (27,803) | - | - | (27,803) |
| Retained earnings/(deficit)/fund balance at end of year (notes 15 and 16) | $ (264,967) | 106,239 | 1,779,389 | 1,620,661 |

See accompanying notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

Combined Statement of Cash Flows -
All Proprietary Fund Types

Year ended June 30, 1991
(In thousands)

| | Proprietary Fund Types | | |
|---|---|---|---|
| | Enterprise | Internal Service | Totals (Memorandum Only) |
| Cash flow from operating activities: | | | |
| Operating income/(loss) | $ (496,270) | 79,449 | (416,821) |
| Adjustments to reconcile operating income/(loss) to net cash provided by operating activities: | | | |
| Depreciation and amortization | 370,194 | 30,917 | 401,111 |
| Provision for uncollectible accounts | 97,714 | 15,864 | 113,578 |
| Amortization of debt discount and issuance costs | 19,297 | 8,735 | 28,032 |
| Net loss on disposition of fixed assets | 2,509 | - | 2,509 |
| Gain on sale of investments | (1,761) | - | (1,761) |
| Amortization of premium on investments | (7,176) | (59,586) | (66,762) |
| Payment of in lieu of taxes | (114,154) | - | (114,154) |
| Net cash flow effect on non-capital financing, capital and related financing and investing activities included in operating income/(loss) | (28,000) | (69,370) | (97,370) |
| Other | (7,997) | 1,880 | (6,117) |
| Changes in assets and liabilities: | | | |
| Increase in: | | | |
| Receivables, net | (62,318) | (259,535) | (321,853) |
| Due from other funds | - | (17) | (17) |
| Inventories | (24,549) | (4,470) | (29,019) |
| Accounts payable and accrued liabilities | 81,891 | - | 81,891 |
| Deposits | 108,606 | - | 108,606 |
| Securities sold under agreements to repurchase | 12,382 | 253,977 | 266,359 |
| Deferred revenue | 5,269 | - | 5,269 |
| Accrued compensated absences | 85,491 | 2,981 | 88,472 |
| Decrease in: | | | |
| Due from other funds | 13,267 | - | 13,267 |
| Restricted assets | 30,432 | - | 30,432 |
| Other assets | 53,380 | 1,019 | 54,399 |
| Accounts payable and accrued liabilities | - | (8,298) | (8,298) |
| Deposits | - | (217,679) | (217,679) |
| Due to other funds | (51,596) | (46,605) | (98,201) |
| Interest payable | (39,927) | (5,097) | (45,024) |
| Other long-term liabilities | (1,514) | (48) | (1,562) |
| Total adjustments | 541,440 | (355,332) | 186,108 |
| Net cash provided by/(used in) operating activities, carried forward | $ 45,170 | (275,883) | (230,713) |

COMMONWEALTH OF PUERTO RICO

Combined Statement of Cash Flows -
All Proprietary Fund Types

Year ended June 30, 1991
(In thousands)

| | Proprietary Fund Types | | |
|---|---|---|---|
| | Enterprise | Internal Service | Totals (Memorandum Only) |
| Net cash provided by/(used in) operating activities, brought forward | $ 45,170 | (275,883) | (230,713) |
| Cash flows from non-capital financing activities: | | | |
| Proceeds from issuance of notes and loans | 453,881 | 599,325 | 1,053,206 |
| Principal paid on notes and loans | (255,883) | (245,411) | (501,294) |
| Interest paid on notes and loans | (68,398) | (78,368) | (146,766) |
| Operating grants received | 145,505 | - | 145,505 |
| Operating transfers in from other funds | 608,394 | 3,000 | 611,394 |
| Operating transfers out to other funds | (41,704) | - | (41,704) |
| Residual equity transfers in from other fund | - | 40,584 | 40,584 |
| Capital contributions | 24,746 | 1,001 | 25,747 |
| Net cash provided by noncapital financing activities | 866,541 | 320,131 | 1,186,672 |
| Cash flows from capital and related financing activities: | | | |
| Acquisition and construction of capital assets | (873,437) | (84,872) | (958,309) |
| Proceeds from issuance of bonds and notes | 403,000 | 4,251 | 407,251 |
| Principal paid on bonds and notes | (206,161) | (22,125) | (228,286) |
| Interest paid on bonds and notes | (296,339) | (65,633) | (361,972) |
| Proceeds from sale of equipment | 69,549 | 2 | 69,551 |
| Capital contributions | 123,833 | - | 123,833 |
| Payment to acquire net assets of Puerto Rico Communications Authority | (76,000) | - | (76,000) |
| Net cash used in capital and related financing activities | (855,555) | (168,377) | (1,023,932) |
| Cash flows from investing activities: | | | |
| Purchase of investments securities | (936,684) | (4,655,267) | (5,591,951) |
| Proceeds from sales and maturities of investments securities | 991,075 | 5,036,697 | 6,027,772 |
| Interest and dividends on investments | 222,166 | 238,384 | 460,550 |
| Net cash provided by investing activities | 276,557 | 619,814 | 896,371 |
| Net increase in cash and cash equivalents | 332,713 | 495,685 | 828,398 |
| Cash and cash equivalents at beginning of year (note (1E)) | 1,533,211 | 1,954,521 | 3,487,732 |
| Cash and cash equivalents at end of year (note (1E)) | $ 1,865,924 | 2,450,206 | 4,316,130 |

See accompanying notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

Combined Statement of Changes in Fund Balance/(Deficit) -
Public University Funds

Year ended June 30, 1991
(In thousands)

| | Current Funds | | | | Plant Funds | | | |
|---|---|---|---|---|---|---|---|---|
| | Unrestricted | Restricted | Loan Funds | Endowment and Similar Funds | Unexpended | Renewal and Replacement | Retirement of Indebtedness | Investment in Plant |
| Revenues and other additions (note 15): | | | | | | | | |
| Unrestricted current fund revenues | $ 328,913 | - | - | - | - | - | - | - |
| Commonwealth grants and contracts | - | 60,882 | - | - | 150 | 1,000 | - | - |
| Federal grants and contracts | - | 84,511 | - | - | 159 | - | 310 | - |
| Private gifts, grants and contracts | - | 9,190 | - | 195 | - | - | - | - |
| Investment income | - | 165 | - | - | 1,727 | - | 1,870 | - |
| Interest on loans receivable | - | - | 117 | - | - | - | - | - |
| Expended for plant facilities (including $4,939 charged to current funds expenditures) | - | - | - | - | - | - | - | 9,642 |
| Retirement of indebtedness | - | - | - | - | - | - | - | 4,599 |
| Other | - | 14,687 | - | - | 2,564 | 194 | - | 705 |
| Total revenues and other additions | 328,913 | 169,435 | 117 | 195 | 4,600 | 1,194 | 2,180 | 14,946 |
| Expenditures and other deductions: | | | | | | | | |
| Educational and general expenditures | 304,460 | 169,539 | - | - | - | - | - | - |
| Auxiliary enterprises expenditures | 7,986 | - | - | - | - | - | - | - |
| Indirect costs recovered | - | 443 | - | - | - | - | - | - |
| Refunded to grantors | - | 56 | 30 | - | - | - | - | - |
| Loan cancellations and assignments | - | - | 16 | - | - | - | - | - |
| Administrative and collection costs | - | - | 28 | - | - | - | - | - |
| Expended for plant facilities | - | - | - | - | 4,366 | 337 | - | - |
| Retirement of indebtedness | - | - | - | - | - | - | 4,599 | - |
| Interest on indebtedness | - | - | - | - | - | - | 13,452 | - |
| Disposal of plant facilities | - | - | - | - | - | - | - | 3,247 |
| Other | - | - | - | - | - | - | - | 984 |
| Total expenditures and other deductions | 312,446 | 170,038 | 74 | - | 4,366 | 337 | 18,051 | 4,231 |
| Transfers among funds-additions/(deductions): | | | | | | | | |
| Mandatory: | | | | | | | | |
| Principal and interest | (16,566) | - | - | - | - | - | 16,566 | - |
| Restricted current fund matching grants | (2,301) | 2,301 | - | - | - | - | - | - |
| Other transfers: | | | | | | | | |
| Unrestricted current funds | (3,999) | 4,522 | - | - | (523) | - | - | - |
| Restricted current funds | 88 | (430) | 60 | 40 | 15 | 227 | - | - |
| Total transfers | (22,778) | 6,393 | 60 | 40 | (508) | 227 | 16,566 | - |
| Net increase/(decrease) for the year | (6,311) | 5,790 | 103 | 235 | (274) | 1,084 | 695 | 10,715 |
| Fund balance/(deficit) at beginning of year | (1,736) | 5,274 | 5,683 | 908 | 5,787 | - | 20,870 | 195,750 |
| Fund balance/(deficit) at end of year | $ (8,047) | 11,064 | 5,786 | 1,143 | 5,513 | 1,084 | 21,565 | 206,465 |

See accompanying notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

Combined Statement of Current Funds Revenues, Expenditures and Other Changes - Public University Funds

Year ended June 30, 1991
(In thousands)

| | Unrestricted | Restricted | Total |
|---|---|---|---|
| Revenues: | | | |
| Tuition and fees | $ 27,184 | 3,003 | 30,187 |
| Federal grants and contracts | - | 82,314 | 82,314 |
| Private gifts, grants and contracts | - | 9,190 | 9,190 |
| Sales and services of educational departments | 1,367 | 1,732 | 3,099 |
| Sales and services of auxiliary enterprises | 5,209 | - | 5,209 |
| Investment income | - | 165 | 165 |
| Other sources | 3,708 | 9,952 | 13,660 |
| Total current revenues | 37,468 | 106,356 | 143,824 |
| Expenditures and mandatory transfers: | | | |
| Educational and general: | | | |
| Instruction | 121,934 | 11,850 | 133,784 |
| Research | 4,441 | 32,876 | 37,317 |
| Public service | 808 | 23,192 | 24,000 |
| Academic support | 40,020 | 936 | 40,956 |
| Student services | 17,061 | 1,830 | 18,891 |
| Institutional support | 68,881 | 947 | 69,828 |
| Operation and maintenance of plant | 44,814 | 532 | 45,346 |
| Scholarships and fellowships | 906 | 63,882 | 64,788 |
| Hospitals | - | 30,656 | 30,656 |
| Independent operations | 361 | 11 | 372 |
| Other | 5,234 | 2,827 | 8,061 |
| Educational and general expenditures | 304,460 | 169,539 | 473,999 |
| Mandatory transfers for: | | | |
| Principal and interest | 16,566 | - | 16,566 |
| Restricted current fund matching grants | 2,301 | (2,301) | - |
| Total educational, general and mandatory transfers | 323,327 | 167,238 | 490,565 |
| Auxiliary enterprises - expenditures | 7,986 | - | 7,986 |
| Total expenditures and mandatory transfers | 331,313 | 167,238 | 498,551 |
| Other transfers and additions/(deductions): | | | |
| Commonwealth grants and contracts | 291,445 | 60,882 | 352,327 |
| Excess of restricted receipts over transfers to revenues | - | 1,754 | 1,754 |
| Refunded to grantors | - | (56) | (56) |
| Non mandatory transfers | (3,911) | 4,092 | 181 |
| Total other transfers and additions/(deductions) | 287,534 | 66,672 | 354,206 |
| Net increase/(decrease) in fund balance | $ (6,311) | 5,790 | (521) |

See accompanying notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO

Notes to General Purpose Financial Statements

June 30, 1991

## (1) Summary of Significant Accounting Policies

The Commonwealth of Puerto Rico (the Commonwealth) was constituted on July 25, 1952, under the provisions of its Constitution as approved by the people of Puerto Rico and the United States Congress. The Commonwealth's Constitution provides for the separation of powers of the executive, legislative and judicial branches of the government. The Commonwealth assumes responsibility for public safety, health, public housing, welfare, education and economic development.

The accompanying general purpose financial statements have been prepared in conformity with generally accepted accounting principles as applicable to governmental units. The following is a summary of the significant accounting policies:

### A. Reporting Entity

In evaluating how to define the Commonwealth for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth by generally accepted accounting principles. The basic, but not the only, criterion for including a potential component unit within the reporting entity is the governing body's ability to exercise oversight responsibility over the component unit. The significant manifestations of this ability include, but are not limited to, financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters. A second criterion used in evaluating potential component units is the scope of public service. Application of this criterion involves considering whether the activity benefits the government and/or its people, or whether the activity is conducted within the geographic boundaries of the government and is generally available to its people. A third criterion used to evaluate potential component units for inclusion or exclusion from the reporting entity is the existence of special financing relationships, regardless of whether the government is able to exercise oversight responsibilities. Based upon the application of these criteria, all departments, agencies and government entities whose funds are by Act No. 230 of July 23, 1974, as amended, under the custody and control of the Secretary of the Treasury, and the following public corporations, executive and government agencies are included in the general purpose financial statements:

Agricultural Development Administration
Agricultural Services Administration
Automobile Accident Compensation Administration
Commercial and Agricultural Credit and Development Corporation of Puerto Rico
Cooperative Development Company of Puerto Rico
Corporation for Technological Development of Tropical Resources of Puerto Rico
Corporation for Technological Transformation
Corporation of Stock and Deposit Insurance for the Savings and Loans Cooperatives
Culebra Conservation and Development Authority
Economic Development Bank for Puerto Rico
Farm Credit Guarantee Fund
Farm Credit Trust Fund
Farm Insurance Corporation
Fine Arts Center Corporation
General Services Administration
Government Development Bank for Puerto Rico and Subsidiaries
Guarantee Loan Fund for Eligible Businesses
Health Facilities and Services Administration of Puerto Rico
Industries for the Blind, for Mentally Retarded and Other Disabled Persons of Puerto Rico
Irrigation Systems of Puerto Rico
Metropolitan Bus Authority
Musical Arts Corporation and Subsidiaries
Office for the Improvement of the Puerto Rico Public Schools
Office of Human Development
Prison Industries Corporation
Public Buildings Authority
Puerto Rico and Caribbean Cardiovascular Center Corporation
Puerto Rico Aqueduct and Sewer Authority
Puerto Rico Electric Power Authority
Puerto Rico Highway and Transportation Authority
Puerto Rico Housing Bank and Finance Agency
Puerto Rico Industrial Development Company and Subsidiaries
Puerto Rico Industrial, Medical, Educational and Environmental Pollution Control Facilities Financing Authority

Puerto Rico Infrastructure Financing Authority
Puerto Rico Land Administration
Puerto Rico Land Authority
Puerto Rico Maritime Shipping Authority
Puerto Rico Medical Services Administration
Puerto Rico Minerals Resources Development Corporation
Puerto Rico Municipal Finance Agency
Puerto Rico Ports Authority
Puerto Rico Public Broadcasting Corporation
Puerto Rico Rural Housing Administration
Puerto Rico Telephone Authority and Subsidiaries
Puerto Rico Urban Renewal and Housing Corporation
Recreational Development Company of Puerto Rico
Right to Employment Administration
Rural Development Corporation of Puerto Rico
Solid Waste Authority of Puerto Rico
Special Fund for Loans to Governmental Entities
State Insurance Fund
Sugar Corporation of Puerto Rico
Tourism Company of Puerto Rico
Trust for the Development, Operation and Conservation of National Parks of Puerto Rico
University of Puerto Rico

The financial information of the entities included in the general purpose financial statements is substantially derived from the most recent audited financial statements and is presented as governmental, proprietary, fiduciary and public university fund categories, as applicable. The Puerto Rico Housing Bank and Finance Agency, Puerto Rico Urban Renewal and Housing Corporation and Tourism Company of Puerto Rico segregate their operations in their separately issued financial statements as governmental and proprietary funds. Such presentation is followed in the accompanying general purpose financial statements. The inclusion of the entities listed above in the general purpose financial statements reflects the oversight role exercised by the Commonwealth but in the case of public corporations does not affect their separate legal standing. Additional information about the entities included in public university funds and proprietary funds is provided in notes 15 and 16.

Municipal governments are not considered part of the Commonwealth's reporting entity since they are accountable to a separately elected legislative body that exercises complete autonomy over their fiscal and institutional matters.

The retirement systems of the University of Puerto Rico, Puerto Rico Electric Power Authority and Puerto Rico Telephone Company, a wholly-owned subsidiary of the Puerto Rico Telephone Authority, are excluded from the reporting entity because these systems exercise control over their financial, operational and personnel matters, and receive no funds from and have no continuing policy-making affiliation with the Commonwealth.

## B. Basis of Presentation

The general purpose financial statements have been prepared primarily from accounts maintained by the Commonwealth's Secretary of the Treasury (the Secretary). Additional data have been derived from reports prescribed by the Secretary and prepared by Commonwealth departments, agencies, public corporations and other entities based on independent or subsidiary accounting systems maintained by them.

The Commonwealth records its transactions in the fund types and account groups described below. Transactions between funds within a fund type, if any, have been eliminated.

### Governmental Fund Types

Governmental funds are used to account for the Commonwealth's expendable financial resources and related liabilities (except those accounted for in proprietary, similar trust and public university funds). The measurement focus is upon determination of and changes in financial position. The following are the Commonwealth's governmental fund types:

**General Fund** - The general fund is the general operating fund of the Commonwealth. It is used to account for all financial transactions except those required to be accounted for in another fund. The operations of the Lottery of Puerto Rico are included in the general fund for financial reporting purposes.

**Special Revenue Funds** - Special revenue funds are used to account for the proceeds of specific revenue sources (other than debt service, expendable trusts or major capital projects) such as Federal grants, that are legally restricted to expenditures for specified purposes.

**Debt Service Funds** - Debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs. Long-term debt and interest due July 1 of the following fiscal year is accounted for as a fund liability if resources are available as of June 30 for its payment.

**Capital Projects Funds** - Capital projects funds are used to account for the financial resources used for acquisition or construction of major capital facilities (other than those financed by proprietary, similar trust and public university funds).

**Proprietary Fund Types**

Proprietary funds are used to account for activities that are similar to those often found in the private sector. The measurement focus is upon determination of net income and capital maintenance. The following are the Commonwealth's proprietary fund types:

**Enterprise Funds** - Enterprise funds are used to account for operations (a) that are financed primarily through user charges, or (b) where the governing body has decided that determination of net income is appropriate.

**Internal Service Funds** - Internal service funds are used to account for goods or services provided by component units or agencies to other component units, departments or agencies.

**Fiduciary Fund Types**

**Trust and Agency Funds** - Fiduciary funds are used to account for assets held by the Commonwealth in a trustee capacity (e.g., endowments and pensions) or as an agent for individuals, private organizations and other funds. Trust funds include expendable and pension trust funds. Pension trust funds are reported in the same manner as proprietary funds. Expendable trust funds are reported in the same manner as governmental funds. Agency funds are custodial in nature and do not involve measurement of results of operations.

**Account Groups**

**General Fixed Assets Account Group** - This account group is used to account for general fixed assets of the Commonwealth exclusive of assets held by the proprietary, similar trust and public university funds.

**General Long-term Debt Account Group** - This account group is used to account for long-term obligations of the Commonwealth including bonds, appropriations and revenue bonds and notes payable, obligations under lease/purchase agreements, and other long-term liabilities exclusive of liabilities of proprietary, similar trust and public university funds.

**Public University Funds**

The public university funds are used to account for the activities of the University of Puerto Rico. Accordingly, the public university funds are an aggregate of the following funds required by existing authoritative accounting and reporting principles applicable to colleges and universities: current funds - restricted and unrestricted, loan funds, endowment and similar funds, and plant funds.

C. **Basis of Accounting**

The basis of accounting determines when the Commonwealth recognizes revenues and expenditures/expenses and related assets and liabilities.

The modified accrual basis of accounting is followed by governmental funds, expendable trust funds and agency funds. Under the modified accrual basis of accounting, revenues are recorded when they become measurable and available to pay liabilities of the current period. Tax revenues are recorded by the Commonwealth as taxpayers earn income (income and other taxes), as taxes are levied (property), as sales are made (consumption and use taxes) and as cash is received (miscellaneous taxes); net of estimated overpayments (refunds). Taxes collected within the following periods after June 30 are recorded as receivables and revenues:

| | |
|---|---|
| Income taxes | 120 days |
| Property and unemployment taxes | 60 days |
| Excise taxes, including Federal excise taxes reimbursed to the Commonwealth | 30 days |

In applying the susceptible to accrual concept to intergovernmental revenues, there are essentially two types of revenues. In one, monies must be expended on the specific purpose or project before any amounts will be paid to the Commonwealth; therefore, revenues are recognized based upon the expenditures incurred. In the other, monies are virtually unrestricted and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenues at the time of receipt or earlier if the susceptible to accrual criteria are met.

Expenditures and related liabilities are recorded in the accounting period in which the liability is incurred, except for (1) interest on long-term obligations, which is recorded when due except for interest due July 1 of the following year which is recorded when resources are available in the debt service funds and (2) vacation, sick leave, Christmas bonus, disallowances and litigation which are recorded in the general long-term debt account group.

The Commonwealth reports deferred revenue on its combined balance sheet. Deferred revenue arises when a potential revenue does not meet both the "measurable" and "available" criteria for recognition in the current period. Deferred revenue also arise when resources are received by the Commonwealth before it has a legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures. In subsequent periods, when both revenue recognition criteria are met, or when the Commonwealth has a legal claim to the resources, the liability for deferred revenue is removed from the combined balance sheet and revenue is recognized.

The accrual basis of accounting is used by proprietary and pension trust funds. Under the accrual basis, revenue is recognized when earned and expenses are recorded as liabilities are incurred, without regard to receipt or payment of cash. The accrual basis is also used by the public university funds except that depreciation of fixed assets is not required to be recorded and that pension contributions are not recorded in accordance with generally accepted accounting principles (see note 15).

D. **Cash and Investments**

Cash balances of funds held by the Secretary of the Treasury (the Secretary) are commingled in a general checking account and several special purpose bank accounts in the Government Development Bank (see note 3). Each fund records its equity interest in the pooled cash balance. The available cash balance in the general checking account beyond immediate needs is invested in interest-bearing accounts with the Government Development Bank. The interest earnings are all credited to the general fund. Cash balances not held by the Secretary are controlled by various Commonwealth officials and deposited in qualified public depositories (see note 2).

Investments are stated at cost or amortized cost.

E. **Statement of Cash Flows**

In September 1989, the Governmental Accounting Standards Board issued Statement No. 9, "Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting" which requires the presentation of a statement of cash flows and certain other disclosures. The Commonwealth adopted this statement in the current year. For purposes of the statement of cash flows, the Commonwealth considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

Certain reclassifications have been made on cash and investments, restricted assets and other assets as of June 30, 1990 to conform with the current year presentation. The reconciliation of cash and cash equivalents in the combined statement of cash flows to the balance sheet is as follows (amounts in thousands):

| | Enterprise Fund | | |
|---|---|---|---|
| | Unrestricted Assets | Restricted Assets | Total |
| Cash and cash equivalents, including amounts in governmental banks | $ 1,476,061 | 389,863 | 1,865,924 |
| Investments | 556,258 | 960,448 | 1,516,706 |
| Other restricted assets | - | 95,819 | 95,819 |
| Total | $ 2,032,319 | 1,446,130 | 3,478,449 |

| | Internal Service Fund | | |
|---|---|---|---|
| | Unrestricted Assets | Restricted Assets | Total |
| Cash and cash equivalents, including amounts in governmental banks | $ 2,431,038 | 19,168 | 2,450,206 |
| Investments | 936,919 | 2,009,291 | 2,946,210 |
| Total | $ 3,367,957 | 2,028,459 | 5,396,416 |

F. **Receivables**

Receivables are stated net of estimated allowances for uncollectible amounts, which are determined based upon past collection experience and current economic conditions. Receivables from the Federal Government represent amounts owed to the Commonwealth for reimbursement of expenditures incurred pursuant to Federally funded programs.

G. **Inventories**

Inventories in proprietary funds are mainly valued at the lower of first-in, first-out cost or market. The governmental and expendable trust funds use the purchase method of accounting which recognizes an expenditure when the inventory is purchased while the proprietary funds recognize an asset when the inventory is purchased and an expense when it is consumed.

H. **Restricted Assets**

Debt proceeds and funds set aside for payments of bonds issued by proprietary funds and funds set aside by the general and special revenue funds for payment and guarantee of notes and interest payable are classified as restricted assets since their use is limited by applicable debt agreements.

I. **General Fixed Assets**

The general fixed assets are recorded as expenditures in the governmental funds and expendable trust funds and capitalized at cost in the general fixed assets account group. Donated fixed assets are recorded at their estimated fair market value at the time received.

Certain improvements such as roads, bridges, curbs and gutters, streets and sidewalks, drainage systems, and lighting systems are not capitalized. Such assets normally are immovable and of value only to the Commonwealth. Therefore, the purpose of stewardship for capital expenditures is satisfied without recording these assets. Depreciation is not provided on general fixed assets.

J. **Fund Fixed Assets**

Fixed assets recorded by proprietary and similar trust funds are stated at cost or estimated historical cost. Contributed fixed assets are recorded at estimated fair market value at the time received. Interest costs are capitalized on projects during the construction period. Depreciation is provided using the straight-line method over estimated useful lives ranging from 25 to 50 years for buildings, 10 to 20 years for improvements other than buildings, and 3 to 10 years for equipment.

K. <u>Tax Refunds Payable</u>

During the calendar year, the Commonwealth collects withholdings and payments from taxpayers for individual income taxes. At June 30, the Commonwealth estimates the amount owed to taxpayers for overpayments during the first half of the calendar year. These estimated amounts are recorded as tax refunds payable and as a reduction of tax revenues.

L. <u>Long-term Debt</u>

The liabilities reported in the general long-term debt account group include the Commonwealth's general obligation bonds and notes, appropriation and revenue bonds and notes payable of component units, due to other funds payable from legislative appropriations, obligations under lease/purchase agreements and other long-term liabilities including vacation, sick leave, Christmas bonus, litigation and disallowances related to expenditures of Federal grants.

M. <u>Reservations of Fund Balance</u>

Reservations of fund balance represent portions of fund balances that are legally segregated for a specific future use or are not appropriable for expenditure. The Commonwealth has the following reservations of fund balance:

**Encumbrances** - Represents future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.

**Debt Service** - Represents net assets available to finance future debt service payments.

**Employees' Retirement** - Represents the public employees' retirement systems net assets available to finance future benefit obligations.

**Unemployment Benefits** - Represents net assets available to fund future unemployment benefits payments.

**Other Specified Purposes** - Represents reservation for monies set aside for guarantee of notes payable, disability, drivers insurance, long-term assets, construction commitments, endowment and amounts available to fund various fiduciary arrangements.

N. Post-Retirement Benefits

In addition to the pension benefits described in note 14, the Commonwealth provides post-retirement health care benefits and a Christmas bonus for its retired employees in accordance with law. Substantially all of the employees may become eligible for these benefits if they reach normal retirement age while working for the Commonwealth. Health care benefits are provided through insurance companies whose premiums are paid by the retiree and by the Commonwealth for a fixed amount of $40 per month for each retiree. During the year ended June 30, 1991, the cost of providing health care benefits amounted to $29.7 million. The Christmas bonus paid to the retired employees during the year ended June 30, 1991 was $150 per retiree and the total amount was $9.3 million. These benefits are recorded as expenditures when paid. The plan covers approximately 62,000 retirees.

O. Compensated Absences

The vacation policy of the Commonwealth generally provides for the accumulation of 2.5 days per month, except for the teachers who accrue 4 days per month. The teachers use their vacation in the months of June and July. Unpaid vacation time accumulated is fully vested to the employees from the first day of work.

Employees accumulate sick leave generally at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated unpaid sick leave at the then current rate, if the employee has at least 10 years of service with the Commonwealth.

General long-term debt includes $213.9 million of accrued sick leave benefits, $226.7 million of accrued vacation benefits, $5.9 million of accrued compensated overtime, representing the Commonwealth's commitment to fund such costs from future operations and $7.3 million of compensated absences pertaining to component units accounted for in governmental funds. Sick leave and vacation benefits are accumulated in the proprietary, similar trust and public university funds in the period they are earned and are included as a fund liability.

P. **Interfund Transactions**

The Commonwealth has the following types of transactions among funds:

**Operating Transfers** - Legally required transfers that are reported when incurred as "Operating transfers in" by the recipient fund and as "Operating transfers out" by the disbursing fund.

**Transfers of Expenditures (Reimbursements)** - Reimbursement of expenditures made by one fund for another that are recorded as expenditures in the reimbursing fund and as a reduction of expenditures in the reimbursed fund.

**Residual Equity Transfers** - Nonroutine or nonrecurring transfers between funds that are reported as additions to or deductions from the fund equity balance.

**Interfund Payments (Quasi-external Transactions)** - Charges or collections for services rendered by one fund to another that are recorded as revenues of the recipient fund and expenditures or expenses of the disbursing fund.

Q. **Lottery of Puerto Rico**

The revenues, expenditures and prizes of the Lottery of Puerto Rico are reported within the General Fund. Monies collected prior to June 30 for tickets sold related to drawings to be conducted subsequent to June 30 are reported as deferred revenue. Unpaid awarded prizes as of June 30 are reported as a fund liability. Lottery tickets sold and earned as of June 30 amounted to $388.9 million and are reported as charges for services in the general fund.

R. **Public University Funds**

Financial activities of the University of Puerto Rico (University) are reported in the public university funds. These funds use generally accepted accounting principles that apply to colleges and universities and are presented in a separate column on the general purpose financial statements as a discrete presentation. The public university funds present the combination of the following funds:

**Current Funds** - Account for resources that may be used for any purpose in carrying out the primary objectives of the University.

**Loan Funds** - Account for resources available for loans to students, faculty, or staff of the University.

**Endowment and Similar Funds** - Account for endowment and quasi-endowment transactions. These funds are similar to trust funds and the University must comply with the terms of any applicable agreements.

**Plant Funds** - Account for transactions involving physical properties of the University. The investment in plant accounts for funds that the University has expended and thus has invested for property and any related outstanding debt.

**Agency Funds** - Account for resources held by the University as custodian or agent for others.

The Combined Statement of Current Funds Revenues, Expenditures and Other Changes - Public University Funds is a statement of financial activities related to the current reporting period. It does not purport to present the results of operations or the net income or loss for the period as would a statement of income or a statement of revenues and expenses.

The measurement focus in the public university funds is upon determination of resources received and used. Current funds used to finance plant assets are accounted for as (1) expenditures, for normal replacement of movable equipment and library books; (2) mandatory transfers, for required provisions for debt amortization/interest and equipment renewal and replacement; and (3) transfers of a nonmandatory nature for all other cases.

Public university funds record expenditures when they acquire fixed assets and capitalize those assets within the plant funds. These funds capitalize interest expenditures during construction but do not record depreciation.

Public university funds use the consumption method of recording inventories.

S. **Deficit Fund Balances**

In addition to the component units with a deficit fund balance that are reported within the proprietary fund category (see note 16), the following component units presented as governmental funds reflect a deficit fund balance within the special revenue fund type (amounts in thousands):

| | |
|---|---|
| Puerto Rico Urban Renewal and Housing Corporation (unaudited) | $ 68,789 |
| Recreational Development Company of Puerto Rico | 40,906 |
| | $ 109,695 |

T. **Claims and Judgments**

The estimated amount of the liability for claims and judgments which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund. The general long-term debt account group includes an amount estimated as a contingent liability or liabilities with a fixed or expected due date which will require future available financial resources for its payment.

U. **Effect of Inclusion of Prior Year Operations**

The financial statements of certain component units included in the accompanying general purpose financial statements are the same as those included in the 1990 general purpose financial statements as such financial statements are the most recent available. Such component units are the Agricultural Services Administration, Cooperative Development Company of Puerto Rico and Farm Insurance Corporation (presented as enterprise fund) and Rural Development Corporation (presented as special revenue fund). Management is of the opinion that the inclusion of the same financial statements does not have a significant effect on the financial statements.

V. **Totals (Memorandum Only) Column**

Totals columns on the combined statements are captioned "Memorandum Only" to indicate that they are presented only to facilitate financial analysis. Data in these columns do not present financial position, results of operations, or changes in financial position in conformity with generally accepted accounting principles. Such data are not comparable to a consolidation since interfund eliminations have not been made.

(2) **Cash, Cash Equivalents and Investments**

The Commonwealth's cash, cash equivalents and investments (excluding proprietary and public university funds) at June 30, 1991 follow (amounts in thousands):

| | Unrestricted | Included in Restricted Assets | Total |
|---|---|---|---|
| Cash and cash equivalents | $ 1,132,106 | 596,024 | 1,728,130 |
| Investments | 1,514,008 | 42,668 | 1,556,676 |
| | $ 2,646,114 | 638,692 | 3,284,806 |

**Cash and Cash Equivalents**

Under Commonwealth statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of Federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury or an agent in the Commonwealth's name. The Commonwealth's deposits with commercial financial institutions amounting to $376.5 million were covered by Federal depository insurance or collateral as of June 30, 1991.

The Commonwealth has $721.5 million on deposit with the United States Government. Such deposit represents unemployment insurance taxes collected from employers which are transferred to the Federal Unemployment Insurance Fund in the U.S. Treasury.

The cash and cash equivalents included in restricted assets is maintained in interest bearing accounts in the Government Development Bank, is uncollateralized and is held for the guarantee and payment of notes and interest payable.

**Investments**

Pursuant to statutory authority, the Secretary of the Treasury may invest in obligations of the United States of America, obligations of the Commonwealth of Puerto Rico or obligations of the municipalities of Puerto Rico. The public corporations and retirement systems may invest in those securities authorized by the legal provisions set forth in their Organic Act; such as stocks, corporate bonds, obligations of the United States, mortgage loans and others.

The following table shows the carrying amount and market value (amounts in thousands) as of June 30, 1991 of investments which are held by component units presented as governmental funds and the retirement systems. All investments are categorized below to give an indication of the level of risk at June 30, 1991. Category 1 includes investments that are insured or registered for which the securities are held or maintain by the component units and retirement system or their agents in the component unit or retirement system's name. Category 2 includes uninsured and unregistered investments for which the securities are held by broker or dealer's trust department or their agents in the component unit or retirement system's name. Category 3 includes investments for which the securities are held by the broker-dealer but not in the component unit or retirement system's name:

| | Category 1 | Category 2 | Category 3 | Carrying Amount | Market Value |
|---|---|---|---|---|---|
| **Unrestricted** | | | | | |
| Common and preferred stocks | $ 560,249 | - | - | 560,249 | 663,981 |
| Corporate bonds | 375,169 | - | - | 375,169 | 378,909 |
| U.S. Government and agencies | 446,224 | - | - | 446,224 | 448,932 |
| Short-term Investments | 70,857 | - | - | 70,857 | 71,252 |
| Mortgage loans | 52,923 | - | - | 52,923 | 48,126 |
| Repurchase agreements | - | - | 8,586 | 8,586 | 8,586 |
| | $ 1,505,422 | - | 8,586 | 1,514,008 | 1,619,786 |
| **Restricted** | | | | | |
| U.S. Government and agencies | - | 1,000 | - | 1,000 | 1,000 |
| Guaranteed investment contracts | - | 41,668 | - | 41,668 | 38,773 |
| | $ - | 42,668 | - | 42,668 | 39,773 |

## (3) Cash, Cash Equivalents and Investments in Governmental Banks

Cash, cash equivalents and investments in governmental banks represents the balance of interest and non-interest bearing accounts in the Government Development Bank (GDB) and the Economic Development Bank (EDB) amounting to $2.52 billion and $80 million, respectively. In addition, restricted assets include cash in GDB and EDB amounting to $834.7 million (see notes 2 and 16). Such cash is received by the banks, commingled with other deposits and retained as cash or used for investments, loans, acquisition of other assets or other uses consistent with the functions of the banks. Accordingly, it is not possible to determine the use of specific deposits from the various Commonwealth funds. The deposit liability is substantially related to deposit from other component units and the Department of the Treasury. Such deposit liability is not in agreement with cash in governmental banks because cash of certain component units is reported at a different fiscal year-end and because of other reconciling items such as outstanding checks and deposits in transit.

GDB is a public corporation of the Commonwealth which is included in the general purpose financial statements as an internal service fund. Its primary responsibilities are to act as fiscal agent for the Commonwealth and its public entities and to make loans principally to public entities which will aid in developing the economy of Puerto Rico.

EDB is a public corporation of the Commonwealth which is included in the general purpose financial statements as an enterprise fund. Its primary responsibility is the promotion of the development of the private sector of the economy of Puerto Rico.

No collateral is maintained for cash in interest bearing accounts in GDB. Collateral is maintained for cash in checking accounts in the name of the Commonwealth's Secretary of the Treasury. At June 30, 1991 securities with a carrying value of $148 million were pledged as collateral for these accounts.

## (4) Receivables

Taxes receivable at June 30, 1991 follow (amounts in thousands):

| | General Fund | Debt Service Funds | Trust and Agency Funds |
|---|---|---|---|
| Income | $ 43,089 | - | - |
| Property | 4,418 | 1,990 | - |
| Excise | 31,710 | - | - |
| Unemployment | - | - | 76,593 |
| | $ 79,217 | 1,990 | 76,593 |

The Commonwealth real and personal property tax is levied each July 1 and May 15, respectively, on the assessed values of the prior January 1, for all properties located in the Commonwealth. Assessed values of real property are established at the estimated current value existing in the year 1957 and of personal property at the current value at the date of the assessment.

Real property taxes are billed by the Commonwealth and are due in two equal installments in July and January following the assessment date. Personal property taxes are self-assessed and are due in May, following the assessment date. Revenue is recorded in the month the taxes are due, provided they are collected during the year or within sixty days following the end of the year.

The property tax rate per annum varies among municipalities; however, 4.03% and 2.03% of real and personal property, respectively, belongs to the Commonwealth and the remainder to the applicable municipality. The amount that belongs to the Commonwealth is recorded in the general fund, except for 1.03% that is restricted for the payment of general obligation bonds and notes and is recorded in the debt service fund. The amount that belongs to the municipality is collected by the Commonwealth and recorded in an agency fund. Such amount is subsequently used to reduce prior advances to the municipality, except for a portion that is kept by the Commonwealth for debt service of the municipality.

Real and personal property tax exoneration is granted by the Commonwealth to owners of real property on the first $15,000 of the assessed value of residential units occupied by the owner and, for the first $50,000 in personal property if the taxpayer does not exceed $150,000 in sales volume. The amount paid by the Commonwealth to the municipalities for this exoneration during the year ended June 30, 1991 was $87 million.

During August 1991, legislation was enacted which transfers the functions of billings and collections of property taxes to a new entity controlled by the mayors of the municipalities. Such legislation eliminates the property tax revenue currently allocated to the general fund of the Commonwealth and reduces certain Commonwealth expenditures commencing with the year ending June 30, 1992.

Loans and advances receivable in the trust and agency fund include loans receivable from participants in the retirement systems as follows (amounts in thousands):

| | |
|---|---|
| Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) | $ 303,066 |
| Puerto Rico Judiciary Retirement System (JRS) | 1,167 |
| Annuity and Pension System for the Teachers of Puerto Rico (TRS) | 214,368 |
| | $ 518,601 |

The above amount, as well as the related escrow liability of $29.4 million, included in other liabilities, is based on estimates as the actual amounts as of June 30, 1991 have not been determined.

The ERS and JRS completed an analysis of each individual loan account through June 30, 1989 resulting in a reduction to the balance as of such date of $67.8 million. Such reduction and an adjustment to the escrow liability was recorded during the year ended June 30, 1991 as a restatement of beginning fund balance for $67.1 million. These systems are continuing the analyses. In addition TRS is also in the process of analyzing each individual loan account to determine the appropriate amount for loans receivable from participants. The adjustment, if any, to be made after all of these analyses are completed, to loans receivable from participants and escrow liability as of June 30, 1991 and related investment earnings through such date is not known.

## (5) General Fixed Assets (Unaudited)

The general ledger maintained by the Department of the Treasury (Department) reflects general fixed assets amounting to $1.7 billion. The Department is in the process of reconciling the subsidiary records of all owned general fixed assets to the general ledger to determine the completeness of such subsidiary records. The general fixed assets account group also includes $530 million pertaining to component units.

The unaudited investment in general fixed assets at June 30, 1991 is as follows (amounts in thousands):

| | |
|---|---|
| Land | $ 145,099 |
| Buildings | 506,612 |
| Equipment | 741,928 |
| Construction in progress | 798,337 |
| Other fixed assets | 72,270 |
| | $ 2,264,246 |

## (6) Short-term Financing

The Commonwealth issues tax and revenue anticipation notes (TRANS) to temporarily provide funds for operations until taxes and revenues are received from taxpayers. These TRANS are payable solely from taxes and revenues in the general fund collected after the date of issuance through June 30. The Secretary of the Treasury is required to maintain these collections in a special fund after certain prior applications. TRANS outstanding at June 30, 1991 amounting to $400 million were issued at a rate of 4.3% and paid on July 30, 1991. The full faith, credit and taxing power of the Commonwealth are not pledged for the payment of principal and interest on these notes.

On June 29, 1990, the Commonwealth obtained a loan of $85 million from GDB, bearing an annual interest at a floating rate equal to the six month London interbank bid quotation rate (LIBID). This loan is payable from the release of certain reserves of the Public Buildings Authority. The loan shall mature and be due and payable on or before January 1, 1992. The full faith, credit and taxing power of the Commonwealth are not pledged for the payment of this loan or the interest thereon.

Changes in short-term financing during the year were as follows (amounts in thousands):

| | Outstanding June 30, 1990 | Issued | Redeemed | Outstanding June 30, 1991 |
|---|---|---|---|---|
| TRANS | $ 550,000 | 400,000 | 550,000 | 400,000 |
| GDB Loan | 85,000 | - | 31,404 | 53,596 |
| | $ 635,000 | 400,000 | 581,404 | 453,596 |
| Short-term portion of Special Promissory Notes (see note 7) | | | | 30,000 |
| | | | | 483,596 |

(7) **Long-term Debt**

**Bonds Payable**

General obligation bonds are backed by the full faith, credit and taxing power of the Commonwealth. Bonds payable outstanding at June 30, 1991 are as follows (amounts in thousands):

| | |
|---|---|
| Term bonds payable through 2020; interest payable semiannually at rates varying from 5% to 7.9% | $ 1,666,585 |
| Serial bonds payable through 2004; interest payable semiannually at rates varying from 4% to 9.6% | 1,119,680 |
| Capital appreciation bonds payable through 2011; no interest rate, yield ranging from 6.9% to 7.8%. Net of unaccreted discount of $322 million | 195,893 |
| Total general obligation bonds | 2,982,158 |
| Other | 333 |
| Total bonds payable | $ 2,982,491 |

The following is a summary of changes in bonds payable for the year ended June 30, 1991 (amounts in thousands):

| | Balance June 30, 1990 | Issued | Discount Accretion (Redeemed) | Outstanding June 30, 1991 |
|---|---|---|---|---|
| Term bonds | $ 1,328,630 | 347,955 | (10,000) | 1,666,585 |
| Serial bonds | 1,093,565 | 153,490 | (127,375) | 1,119,680 |
| Capital apprecia-tion bonds | 159,308 | 23,552 | 13,033 | 195,893 |
| Serial and demand bonds | 275,000 | - | (275,000) | - |
| Bond anticipation notes | 250,000 | - | (250,000) | - |
| Other | 376 | - | (43) | 333 |
| | $ 3,106,879 | 524,997 | (649,385) | 2,982,491 |

Debt service requirements for general obligation bonds in future years, which are substantially financed by transfers from the general fund, are as follows (amounts in thousands):

| Year ending June 30 | Principal | Interest | Total |
|---|---|---|---|
| 1992 | $ 149,795 | 181,495 | 331,290 |
| 1993 | 156,475 | 171,777 | 328,252 |
| 1994 | 156,600 | 161,987 | 318,587 |
| 1995 | 160,840 | 152,041 | 312,881 |
| 1996 | 167,230 | 141,364 | 308,594 |
| Thereafter | 2,513,302 | 1,252,810 | 3,766,112 |
| | 3,304,242 | 2,061,474 | 5,365,716 |
| Less unaccreted discount | 322,084 | | |
| General obligation bonds | $ 2,982,158 | | |

The above serial and demand bonds were issued by the Puerto Rico Public Finance Corporation (PRPFC) and were paid from the collections by PRPFC of notes payable by Sugar Corporation of Puerto Rico (SCPR) to PRPFC. Such notes are paid from legislative appropriations on behalf of SCPR.

During the year ended June 30, 1991, $25 million of the above bonds were paid and $50 million are recorded as a fund liability at June 30, 1991. The Puerto Rico Public Finance Corporation (PRPFC) sold $200 million notes of the Sugar Corporation of Puerto Rico to a trust established for such purpose. The proceeds received by PRPFC from the sale of such notes were used to defease the remaining serial and demand bonds of $200 million. To finance the purchase of such notes the trust issued tax exempt custodial receipts (TXRs) evidencing ownership of, and rights to receive, specific future principal and interest on such notes issued by the Sugar Corporation of Puerto Rico. Such notes are payable through 1994 from Commonwealth legislative appropriations and accordingly, are presented as notes payable in the general long-term debt account group (see note 16 under Sugar Corporation of Puerto Rico).

Act No. 269 of May 11, 1949, as amended, provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exempt from taxation. The proceeds of said tax are required to be credited to the debt service fund for payment of debt service on general obligation bonds and notes of the Commonwealth.

The Constitution of Puerto Rico provides that direct obligations of the Commonwealth evidenced by full faith and credit bonds or notes shall not be issued if the amount of the principal of and interest on such obligations and on all such obligations theretofore issued which is payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceeds 15% of the average annual revenues of the Commonwealth in the two preceding fiscal years. The Constitution does not limit the amount of debt that the Commonwealth may guarantee (see note 9) so long as the 15% limitation is not exceeded. Currently, the Commonwealth has not been called to make any payments pursuant to guarantees.

Future maximum annual debt service together with the amount paid in the preceding fiscal year under the Commonwealth's guaranty is $341 million. This amount represents 10.26% of the unaudited average annual internal revenues of $3.3 billion for the two preceding fiscal years.

The Commonwealth is in compliance with the above limitation at June 30, 1991.

**Notes Payable**

Notes payable, included in the general long-term debt account group consist of the following at June 30, 1991 (amounts in thousands):

| | |
|---|---|
| Special promissory notes | $ 150,000 |
| Notes payable | 200,000 |
| Total | $ 350,000 |

Special promissory notes for $210 million were issued on June 29, 1989 by the Commonwealth. These notes are payable from the revenues received from taxes levied, due and to be collected by the Commonwealth and revenues segregated pursuant to joint resolution number 3 approved on October 16, 1985. Such resolution was enacted to reimburse advances made to certain entities in previous fiscal years.

These notes bear interest at a percentage that varies from 82.5% to 85% of the applicable London interbank bid quotation rate (LIBID) but not to exceed 12% per annum. Interest is payable quarterly commencing October 1, 1989.

The full faith, credit and taxing power of the Commonwealth are not pledged for the payment of the notes and interest thereon, and the notes are not general obligations of the Commonwealth. Restricted assets in the general fund include $157.4 million of interest bearing accounts held as guarantee of these notes. Debt service requirements for the principal of these notes are as follows (amounts in thousands):

| Year ending June 30 | |
|---|---|
| 1992 (presented in general fund - see note 6) | $ 30,000 |
| 1993 | 30,000 |
| 1995 | 90,000 |
| 1996 | 30,000 |
| Total presented as general long-term debt | 150,000 |
| | $ 180,000 |

Notes payable represent a debt of the Sugar Corporation of Puerto Rico, bearing interest at 11% and which are being paid from legislative appropriations on behalf of the Sugar Corporation of Puerto Rico. Debt service requirements in future years are as follows (amounts in thousands):

| Year ending June 30 | Principal | Interest | Total |
|---|---|---|---|
| 1992 | $ 60,000 | 22,000 | 82,000 |
| 1993 | 65,000 | 15,400 | 80,400 |
| 1994 | 75,000 | 8,250 | 83,250 |
| | $ 200,000 | 45,650 | 245,650 |

**Due to Other Funds**

As of June 30, 1991, the general long-term debt account group reports a liability to the Puerto Rico Electric Power Authority (PREPA), amounting to $129.9 million related to fuel adjustments subsidies granted to residential customers and to the reimbursements of certain costs incurred by the irrigation and rural systems administered by PREPA. This amount is accounted for by PREPA in the enterprise fund as due from other funds. Commencing in the year ending June 30, 1993, the amount related to subsidies of $94.9 million will be paid in installments of approximately $6.3 million over a fifteen-year period. No interest will be paid on this debt. The amount related to the systems of $35 million will be reduced from the required contribution of in lieu of taxes due by PREPA to the Commonwealth.

**Prior Years Defeasance of Debt**

In prior years, the Commonwealth defeased certain general obligation bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Commonwealth's financial statements. At June 30, 1991, $1 billion of bonds outstanding are considered defeased.

## (8) Appropriation and Revenue Bonds and Notes Payable of Component Units

The general long-term debt account group includes debt issued by certain component units, and which is presented by such component units in their financial statements in the general long-term debt account group.

The debt is being paid from legislative appropriations in accordance with enacted laws or joint resolutions approved by the Legislature of the Commonwealth or from internally generated revenues. This debt does not constitute an obligation or pledge of the full faith, credit and taxing power of the Commonwealth. The bonds payable from legislative appropriations have been paid from such appropriations and it is expected that they will continue to be paid from future appropriations.

Changes during the year on the above debt were as follows (amounts in thousands):

| | Outstanding beginning of year | Issued | Redeemed | Outstanding end of year |
|---|---|---|---|---|
| Appropriation Bonds: | | | | |
| Puerto Rico Housing Bank and Finance Agency | $ 345,900 | - | 11,820 | 334,080 |
| Recreational Development Company of Puerto Rico | 2,079 | - | 590 | 1,489 |
| Revenue Bonds and Notes: | | | | |
| Puerto Rico Highway and Transportation Authority | 675,350 | 234,415 | 84,220 | 825,545 |
| Puerto Rico Infrastructure Financing Authority (PRIFA) | 317,175 | - | 11,455 | 305,720 |
| Other | 16,123 | - | 8,768 | 7,355 |
| | $ 1,356,627 | 234,415 | 116,853 | 1,474,189 |

In prior years, certain of the above component units defeased certain bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Commonwealth's financial statements. At June 30, 1991, $103 million of bonds outstanding are considered defeased.

The Act which created PRIFA requires that in the fiscal year ended June 30, 1990, and in each of the following twenty-eight fiscal years, the first $40 million, of Federal excise taxes received by the Commonwealth be transferred to PRIFA for deposit to PRIFA's infrastructure fund (Infrastructure Fund). The maximum principal and interest requirements on the bonds in any fiscal year is $37 million. Federal excise taxes consist of taxes received by the Commonwealth from the United States in connection with rum and other articles subject to Federal excise tax produced in Puerto Rico and sold in the United States. Rum is the only article currently produced in Puerto Rico subject to Federal excise tax, the proceeds of which are required to be transferred to the Commonwealth.

The Federal excise taxes securing the bonds are subject to a number of factors, including the continued imposition and remittance of such taxes to the Commonwealth and conditions affecting the Puerto Rico rum industry. If the Federal excise taxes received by the Commonwealth in any fiscal year are insufficient to deposit $40 million into the Infrastructure Fund, the Act requires that the Authority request and the Budget Director include in the budget of the Commonwealth for the corresponding fiscal year the appropriation needed to cover such insufficiency. The Commonwealth Legislature, however, is not legally obligated to make the necessary appropriation to cover such insufficiency.

Following is a summary of the debt service requirements of appropriation and revenue bonds and notes payable (amounts in thousands):

| | Principal | Interest | Total |
|---|---|---|---|
| First year | $ 53,259 | 104,077 | 157,336 |
| Second year | 54,312 | 100,672 | 154,984 |
| Third year | 57,110 | 97,085 | 154,195 |
| Fourth year | 62,015 | 93,255 | 155,270 |
| Fifth year | 66,561 | 90,730 | 157,291 |
| Thereafter | 1,180,932 | 730,984 | 1,911,916 |
| | $ 1,474,189 | 1,216,803 | 2,690,992 |

The fund balance in the debt service fund includes $183.2 million of component unit fund balance reserved for the payment of the above debt.

## (9) Guaranteed and Appropriation Debt

### Guaranteed Debt

The Commonwealth may provide guarantees for the repayment of certain borrowings of component units to carry out designated projects. At June 30, 1991, the following component unit debts are guaranteed by the Commonwealth (amounts in thousands):

| | Maximum Guarantee | Outstanding Balance |
|---|---|---|
| Public Buildings Authority | $ 1,200,000 | 989,042 |
| Government Development Bank for Puerto Rico | 550,000 | 317,000 |
| Puerto Rico Urban Renewal and Housing Corporation | 325,000 | 99,930 |
| Puerto Rico Maritime Shipping Authority | 60,000 | 60,000 |
| Sugar Corporation of Puerto Rico | 150,000 | - |
| | $ 2,285,000 | 1,465,972 |

The Farm Credit Security Fund, administered by the Commercial and Agricultural Credit and Development Corporation of Puerto Rico, has guaranteed, under the full faith, credit and taxing power of the Commonwealth, certain loans made by private institutions and Farm Credit Corporation (former component unit liquidated on August 1990). This Fund guarantees loans of $26.7 million as of June 30, 1991.

The Puerto Rico Housing Bank and Finance Agency insures mortgages granted to low and moderate income families through its mortgage loan insurance program. The Commonwealth guarantees up to $75 million of such mortgage loans. As of June 30, 1991, the mortgage loan insurance program was insuring loans aggregating $260.7 million and had not issued any debenture bonds.

Currently, the Commonwealth has not been called to make any direct payments pursuant to the above guarantees.

The Commonwealth has guaranteed the payments of rentals of its departments, agencies and component units to the Public Buildings Authority (PBA) under various lease agreements executed pursuant to the law that created PBA. Such rental payments include the amounts required by PBA for the payment of principal of and interest on the guaranteed debt. The rental commitment as of June 30, 1991 for the next five years follows (amounts in thousands):

| Year ending June 30 | |
|---|---|
| 1992 | $ 168,117 |
| 1993 | 182,930 |
| 1994 | 194,714 |
| 1995 | 207,636 |
| 1996 | 217,755 |

**Appropriation Debt**

Certain component unit debt is supported by Commonwealth appropriations. The following represents the outstanding balances of debt payable by appropriations as set forth in enacted legislation of the Commonwealth at June 30, 1991 (amounts in thousands):

| | |
|---|---|
| Puerto Rico Housing Bank and Finance Agency | $ 422,760 |
| Sugar Corporation of Puerto Rico | 271,857 |
| Puerto Rico Urban Renewal and Housing Corporation | 242,112 |
| Health Facilities and Services Administration of Puerto Rico | 323,925 |
| Economic Development Bank for Puerto Rico | 24,000 |
| Puerto Rico Rural Housing Administration | 5,070 |
| | $ 1,289,724 |

The above debt is presented as follows in the general purpose financial statements (amounts in thousands):

| | |
|---|---|
| Debt service fund | $ 54,745 |
| Enterprise fund | 678,717 |
| General long-term debt account group: | |
| Notes payable (tax exempt receipts) | 217,112 |
| Bonds payable | 339,150 |
| | $ 1,289,724 |

Additional special annual appropriations are made to certain component units to enable them to pay their debts. The following represents the outstanding debt at June 30, 1991 which debt is being paid on a yearly basis by annual appropriations of the Commonwealth (amounts in thousands):

| | |
|---|---|
| Puerto Rico Aqueduct and Sewer Authority | $ 61,470 |
| Commercial and Agricultural Credit and Development Corporation of Puerto Rico | 40,000 |
| Metropolitan Bus Authority | 26,617 |
| Puerto Rico Urban Renewal and Housing Corporation | 22,510 |
| Agricultural Services Administration | 7,468 |
| Tourism Company of Puerto Rico | 5,900 |
| General Services Administration | 5,000 |
| Cooperative Development Company of Puerto Rico | 1,400 |
| Public Buildings Authority | 5 |
| | $ 170,370 |

## (10) Obligations under Lease/Purchase Arrangements

The Commonwealth is obligated under capital leases that expire through 2016 for buildings used by certain Commonwealth departments. At June 30, 1991, the capitalized cost of the buildings amounted to $20.8 million and are included in the general fixed assets account group.

The present values of future minimum capital lease payments as of June 30, 1991, included in other long-term liabiities in the general long-term debt account group follow (amounts in thousands):

| Year ending June 30 | |
|---|---|
| 1992 | $ 2,699 |
| 1993 | 2,715 |
| 1994 | 2,731 |
| 1995 | 2,754 |
| 1996 | 2,772 |
| Thereafter | 49,244 |
| Total minimum lease payments | 62,915 |
| Less amount representing interest | 42,049 |
| Present value of minimum lease payments | $ 20,866 |

The Commonwealth is also committed under numerous operating leases, excluding those with the Public Buildings Authority (see note 9), covering real property and equipment. Rental expenditures within the general fund for the year ended June 30, 1991, under such operating leases are $22.1 million. Following is a summary of the future minimum rental commitments under noncancellable real property and equipment leases with terms exceeding one year (amounts in thousands):

| Year ending June 30 | |
|---|---|
| 1992 | $ 26,168 |
| 1993 | 22,727 |
| 1994 | 12,921 |
| 1995 | 5,861 |
| 1996 | 3,359 |
| Thereafter | 2,969 |
| Total | $ 74,005 |

## (11) Interfund Transactions

### Due From/To Other Funds

Interfund receivables and payables generally reflect temporary loans, billings for services provided and recovery of expenditures. The amount reported in the general fund as due from other funds arises primarily from property taxes collections made by an agency fund, overdraft in the pooled cash balance in the special revenue and internal service fund amounting to $62.3 million, $31 million and $15 million, respectively. Due to other funds in the general fund arises primarily from amounts due to enterprise fund and trust and agency fund which amounted to $32 million and $30 million, respectively. Due from other fund in the special revenue fund mainly arise from legislative appropriation due from the general fund for $42 million. Due to other fund in special revenue fund are mainly due to an overdraft in the pooled cash and amounts reported by the Puerto Rico Urban Renewal and Housing Corporation of $31 million and $67 million, respectively. Due from other funds in the enterprise fund are mainly related with the electric power subsidy and reimbursable cost of the irrigation and other systems amounting to $129.9 million, recorded in the general long-term debt account group. The due from other funds is not in agreement with the due to other funds mainly because of different fiscal years.

**Operating Transfers**

The significant operating transfers for the year ended June 30, 1991 include the annual appropriation of the general fund to the debt service fund amounting to $323 million. In addition, the general and capital projects funds made operating transfers of $681 million and $24 million, respectively, to subsidize the operations of and provide capital contributions to certain public corporations and executive agencies recorded primarily within the enterprise fund (see note 16). These amounts differ from operating transfers from other funds due to different fiscal years end and/or certain operating transfers reported as contributed capital.

**Residual Equity Transfers**

During the year the net assets of the Special Fund for Loans to Governmental Entities amounting to $40.6 million administered by the general fund were transferred to the Government Development Bank. The transaction was recorded as a redidual equity transfer out in the general fund and residual equity transfer in, in the internal service fund. On May 30, 1990, the Puerto Rico Telephone Authority (PRTA) acquired the net assets of the Puerto Rico Communications Authority for a payment of $76 million recorded in the general fund as a residual equity transfer in, in the general purpose financial statements of the Commonwealth for the year ended June 30, 1990, since such payment was received by the general fund during such year. However, since the payment is recorded in the PRTA financial statement included herein (see note 16), it is adjusted and reflected as a residual equity transfer out in the enterprise fund.

(12) **Budgetary Basis Reporting**

The Governor of the Commonwealth of Puerto Rico is required by the Constitution to submit to the Legislature an annual budget of capital improvements and operating expenses of the Commonwealth. Such annual budget includes an estimate of revenues and other resources. Public hearings are conducted by the Legislature to obtain public comments on the proposed budget. The Legislature may amend the budget but may not increase any items so as to cause a deficit without imposing taxes to cover such deficit. The Constitution provides that the appropriations made for any fiscal year shall not exceed the total revenues, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law.

The annual budget is legally adopted through passage of an annual appropriation act known as the Joint Resolution of the General Budget. This appropriated budget includes general fund appropriations for recurring ordinary functions of the Commonwealth and for contributions to public corporations, municipalities and private organizations. General fund appropriations for special operating expenses and for capital expenditures are authorized for one or more years.

The Commonwealth prepares its budget on a basis of accounting that differs from generally accepted accounting principles (GAAP). The major differences between the budgetary basis of accounting used in the annual budget and GAAP are the following:

(1) Revenues are recorded when received in cash (budget) as opposed to when susceptible to accrual (GAAP);

(2) Pension expenditures are recorded when payments are made to the various pension systems (budget) as opposed to when the liability is incurred (GAAP); and

(3) Encumbrances are recorded as a segregation of appropriations (budget) as opposed to a reservation of fund balance (GAAP).

A combined statement of revenues and expenditures - budget and actual - general fund, as required by generally accepted accounting principles, is not presented in the general purpose financial statements as the existing accounting programs do not provide for a comparison of approved budgeted amounts with actual results of operations. The Commonwealth is in the process of modifying the existing programs which will permit the presentation of this statement in future years. Budgetary control is maintained at the department or agency level for each individual appropriation.

## (13) Commitments and Contingencies

The Commonwealth receives financial assistance from the Federal Government in the form of grants and entitlements, including several non-cash programs. Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable Federal regulations, including the expenditure of resources for eligible purposes. Substantially all grants are subject to either the Federal Single Audit Act or to financial and compliance audits by grantor agencies. Disallowances as a result of these audits may become liabilities of the Commonwealth. At June 30, 1991, the Commonwealth has recorded liabilities of $3.6 million based on an evaluation of pending disallowances and are reported in the general long-term debt account group.

The Commonwealth is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1955, as amended, persons are authorized to sue the Commonwealth only for causes of actions set forth in said Act to a maximum amount of $75,000 or $150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Commonwealth may provide its officers and employees with legal representation as well as assume the payment of any judgment that may be entered against them. There is no maximum amount on the payment of such judgment.

With respect to pending and threatened litigation, the Commonwealth has reported liabilities of $81 million for awarded and anticipated unfavorable judgments. The portion of the liability which is due on demand, such as from adjudicated or settled claims, amounted to $32 million and is recorded in the general fund. The amount of $49 million included in the general long-term debt account group represents the amount estimated as a probable liability or a liability with a fixed or expected due date which will require future available financial resources for its payment. Management believes that the ultimate liability in excess of amounts provided would not be significant.

In 1979, various inmates under the custody of the Administration of Corrections of the Commonwealth filed a complaint in the United States District Court for the District of Puerto Rico (Court) alleging that the conditions of confinement violated their rights under the United States and the Commonwealth's Constitution. In 1980, the Court rendered an order requiring that the Commonwealth provide a fixed living space per inmate. Since July 1987, the Court has imposed daily fines to the Commonwealth because of its noncompliance with the order amounting to $76 million through June 30, 1991. During the year ended June 30, 1991, the Commonwealth has incurred fines of $46.5 million which are recorded as expenditures of the general fund.

During December 1991, a stipulation was entered into between the inmates and the Commonwealth. Based on such stipulation fines will be paid through November 27, 1991; thereafter they will be calculated only, but will be permanently discharged if the Commonwealth for six consecutive months complies with the terms of the stipulation. The fines paid by the Commonwealth are being maintained in a fund by the Federal Government and will be available to the Commonwealth for authorized projects related to confinement. The stipulation authorizes the Court to release a portion of fine funds to finance certain costs for two projects related to confinement.

Puerto Rico Highway and Transportation Authority's construction commitments as of June 30, 1991 amounted to $317.3 million.

## (14) Retirement Systems

The Commonwealth has three contributory defined benefit pension plans:

- Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS),
- Puerto Rico Judiciary Retirement System (JRS), and
- Annuity and Pension System for the Teachers of Puerto Rico (TRS).

The annual financial statements of each system are presented in the fiduciary funds.

The systems provide retirement, death and disability benefits and annuities to Commonwealth employees, public school employees, and employees of municipalities and certain public corporations not covered by their own systems. These benefit provisions are established by law.

Each system is independent. Assets may not be transferred from one system to another or used for any purpose other than to benefit each system's participants.

The membership at June 30, 1989 of ERS and JRS and at June 30, 1990 of TRS consisted of:

| | ERS | JRS | TRS |
|---|---|---|---|
| Retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits, but not yet receiving benefits | 45,759 | 161 | 20,160 |
| Current employees: | | | |
| Vested | 72,088 | 138 | 23,106 |
| Nonvested | 64,563 | 87 | 21,360 |
| Total members | 182,410 | 386 | 64,626 |

**Funding and Benefit Policies**

The Employees' Retirement System (ERS) is the administrator of an agent multiple-employer retirement system established by the Commonwealth. ERS covers all employees of the Commonwealth and its instrumentalities and of certain municipalities and public corporations not covered by their own systems. Membership is required as a condition of employment.

Retirement and related benefits provided by the system and required contributions to the system by employees are determined by Act 447, approved May 15, 1951, as amended. Required contributions by the Commonwealth are determined by the Administrator of the System. The members contributions are 5.775% or 8.275% and Commonwealth contributions are 9.275% of gross salary.

The amount contributed by the Commonwealth for the year ended June 30, 1991 was $135.6 million. Payroll covered for the year was $1.5 billion.

Members who have attained an age of at least fifty-five (55) years and have completed at least twenty-five (25) years of creditable service or members who have attained an age of at least fifty-eight (58) years and have completed at least ten (10) years of creditable service, are entitled to an annual benefit, payable monthly for life.

The amount of the annuity shall be one and one-half percent of the average compensation multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation multiplied by the number of years of creditable service in excess of twenty years. In no case will the annuity be less than $2,400.

Participants who have completed at least thirty years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained fifty-five (55) years of age will receive 65% of the average compensation or if they have attained fifty-five (55) years of age will receive 75% of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten (10) years of service.

Act Number 1 of 1990 made certain amendments applicable to new participants joining the System effective April 1, 1990. Changes mainly consisted of an increase in the retirement age from 55 to 65, decrease in the benefit percentage of the average compensation in the disability and death benefits annuities from 50% to 40% and the elimination of the Merit Annuity for participants who have completed thirty years of creditable service.

The Judiciary Retirement System (JRS) is administered by the ERS. This system provides pensions and other benefits to the judges of the Commonwealth. For the year ended June 30, 1991 members and Commonwealth contributions were 7.5% and 20% of gross salary, respectively. The amount contributed by the Commonwealth for the year ended June 30, 1991 was $2.2 million. Payroll covered for the year was $11 million.

Participants are entitled to a retirement pension if they have reached the age of sixty (60) or more and shall have at least ten (10) years of creditable service. The retirement pension of any participant shall be equal to 25% of average salary during the last three years of creditable service plus 25/72 of one percent of the said average salary during the last three years for each month of creditable service in excess of ten (10) years of service. The retirement pension shall not exceed 75% of the average salary for the last three (3) years.

The system also provides occupational and non-occupational disability pensions. Participants must have at least ten (10) years of creditable service to be eligible for a non-occupational disability pension.

The Annuity and Pensions System for the Teachers of Puerto Rico provides retirement benefits to all teachers of the Department of Education of the Commonwealth, those holding positions on the Retirement Board, all pensioned teachers, all teachers transferred to an administrative position in the Department of Education, teachers who work in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education. Act No. 218, approved May 6, 1951, as amended, prescribes requirements relating to membership, benefits and contributions.

Members and Commonwealth contributions for the year ended June 30, 1991 were 7% and 8.5% of total salary, respectively. The contributed amount for the year ended June 30, 1991 was $53 million. Payroll covered for the year was $623 million. The system grants retirement benefits to those members who have practiced for a period of twenty-five (25) years and attained the age of fifty-two (52).

Teachers are entitled to a life annuity which consists of a pension, of a sum sufficient, when joined with the annuity, to yield a life annuity equal to 1.71% of the highest average salary over three (3) years, multiplied by the number of years of service rendered.

**Actuarial Cost Methods and Assumptions**

The projected unit credit actuarial cost method was used by the three retirement systems.

The following assumptions were used in the actuarial valuations:

| | ERS | JRS | TRS |
|---|---|---|---|
| Investment rate of return per year | 9% | 9% | 8% |
| Salary increases | 6% | 6% | 6% |
| Mortality rates table | GA '51 | GA '51 | GA '83 |

The valuations of ERS and JRS are based on an actuarial valuation performed as of June 30, 1989. The valuation of TRS is based on an actuarial valuation as of June 30, 1990. There are no valuations for a more recent date.

**Actuarial Present Value of Benefit Obligation**

The unfunded benefit obligation to retirees, beneficiaries, and terminated employees not yet receiving benefits and for current employees for each retirement system is presented below (amounts in millions).

The projected benefit obligation is the actuarial present value at valuation date of all benefits attributed by the pension benefit formula to employees service rendered prior to such date. The projected benefits obligation is measured using assumptions as to future compensation levels.

The pension benefit obligation follows:

| | ERS | JRS | TRS |
|---|---|---|---|
| Pension benefit obligation: | | | |
| Retirees, beneficiaries and terminated employees not yet receiving benefits | $ 1,835 | 23.5 | 918.6 |
| Current employees: | | | |
| Vested | 2,049 | 18.5 | 631.7 |
| Nonvested | 125 | 1.2 | 446.8 |
| Total pension benefit obligation | 4,009 | 43.2 | 1,997.1 |
| Net assets available for benefits, at market value for ERS and JRS and at cost for TRS | 628 | 25.1 | 969.5 |
| Unfunded pension benefit obligation | $ 3,381 | 18.1 | 1,027.6 |

### Contributions Made and Actuarial Computation

Contributions in 1991 and prior years were made based on percentages established by the administrators of the systems. Such percentages have not been based on actuarial studies as required by generally accepted accounting principles. An actuarial computation of the annual contribution applicable to the Commonwealth have not been prepared. Accordingly, the amounts by which the actual contributions are under the required actuarial contribution are not known.

### Trend Information (unaudited)

Trend information gives an indication of the progress made in accumulating sufficient assets to pay benefits when due. Trend information for the available years is as follows (amounts in million):

| | ERS | JRS | TRS |
|---|---|---|---|
| Net assets available for benefits (at market value for ERS and JRS and at cost for TRS): | | | |
| June 30, 1990 | N/A | N/A | 969.5 |
| June 30, 1989 | 628 | 25.1 | N/A |
| June 30, 1988 | 597 | 22.3 | N/A |
| Pension benefit obligation: | | | |
| June 30, 1990 | N/A | N/A | 1,997.1 |
| June 30, 1989 | 4,009 | 43.2 | N/A |
| June 30, 1988 | 3,570 | 47.7 | N/A |
| Unfunded pension benefit obligation: | | | |
| June 30, 1990 | N/A | N/A | 1,027.6 |
| June 30, 1989 | 3,381 | 18.1 | N/A |
| June 30, 1988 | 2,973 | 25.4 | N/A |
| Annual covered payroll: | | | |
| June 30, 1991 | 1,500 | 11.0 | 623 |
| June 30, 1990 | 1,300 | 11.8 | 603 |
| June 30, 1989 | 1,300 | 10.7 | 505 |
| Net assets available for benefits as a percentage of total pension benefit obligation: | | | |
| June 30, 1990 | N/A | N/A | 48.5% |
| June 30, 1989 | 16% | 58% | N/A |
| June 30, 1988 | 17% | 47% | N/A |

| | | | |
|---|---|---|---|
| Unfunded pension benefit obligation as a percentage of annual covered payroll: | | | |
| June 30, 1990 | N/A | N/A | 170% |
| June 30, 1989 | 260% | 169% | N/A |
| June 30, 1988 | 194% | 242% | N/A |
| Employer contributions (not actuarially determined) as a percentage of annual covered payroll: | | | |
| June 30, 1991 | 9.3% | 20% | 8.5% |
| June 30, 1990 | 8.3% | 20% | 8.5% |
| June 30, 1989 | 7.7% | 20% | 8.9% |

N/A = Not available

Analysis of the dollar amounts of net assets available for benefits, pension/accumulated benefit obligation, and unfunded pension/ accumulated benefit obligation in isolation can be misleading. Expressing the net assets available for benefits as a percentage of the pension/accumulated benefit obligation provides one indication of Commonwealth funding status on a going-concern basis. Analysis of this percentage over time indicates whether the system is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the retirement system. Trends in the unfunded pension/ accumulated benefit obligation and annual covered payroll are both affected by inflation. Expressing the unfunded pension/accumulated benefit obligation as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of Commonwealth progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the retirement system.

Revenues by source and expenses by type for the three retirement systems for the available years is as follows (amounts in thousands):

| | Revenues by Source | | | |
|---|---|---|---|---|
| | Employee Contributions | Employer Contributions | Investment Earnings | Total |
| June 30, 1991 | $ 174,895 | 211,441 | 173,720 | 560,056 |
| June 30, 1990 | 142,451 | 178,108 | 146,565 | 467,124 |
| June 30, 1989 | 127,160 | 172,079 | 133,822 | 433,061 |

| | Expenses by Type | | |
|---|---|---|---|
| | Benefits Paid | Administrative Expense | Total |
| June 30, 1991 | $ 371,136 | 32,507 | 403,643 |
| June 30, 1990 | 341,553 | 33,348 | 374,901 |
| June 30, 1989 | 333,652 | 26,228 | 359,880 |

(15) Public University Funds

The University of Puerto Rico (University) was created in 1903 as an institution of higher education primarily to educate citizens; to train students in the professions, arts and sciences; to promote research and creative work; and to assist the community in various technical and academic endeavors.

Commonwealth appropriations are the principal source of revenues, but additional revenues are derived from tuition, student fees, auxiliary enterprises, interest income, federal grants and other sources. The high level of financial support received by the University from the Commonwealth is supported by Act No. 2 of January 20, 1966. Under the Act, the Commonwealth appropriates for the University an amount equal to 9% of the average total amount of annual revenues collected under the laws of the Commonwealth in the two fiscal years immediately preceding the current fiscal year. Much smaller amounts of Commonwealth appropriations for current operations are received under various laws which assign certain percentages of Commonwealth revenues obtained from horse race prizes and certain percentages of net income from slot machine franchises. In addition, the Commonwealth has appropriated in recent years additional amounts for general current operations, capital improvement program, and for loans and financial assistance to students.

Public university funds are comprised of the financial activities of the University. All the financial data were derived from the audited financial statements as of June 30, 1990 (latest available).

The following is a summary of significant information of the University:

**Cash, cash equivalents and Investments**

The University's cash, cash equivalents and investments follow (amounts in thousands):

| | Unrestricted | Included in Restricted Assets | Total |
|---|---|---|---|
| Cash and cash equivalents | $ 29,795 | 3,673 | 33,468 |
| Investments | 958 | 21,377 | 22,335 |
| | $ 30,753 | 25,050 | 55,803 |

The University is authorized to deposit only in financial institutions approved by the Department of the Treasury of the Commonwealth and all cash was maintained in such institutions.

The authorized depositories collateralize cash received with securities that are pledged with the Department of the Treasury. Collateral for cash follows (amounts in thousands):

| | |
|---|---|
| Insured by Federal insurance corporations | $ 343 |
| Collateralized by securities pledged with the Department of the Treasury | 33,082 |
| Uncollateralized | 43 |
| Total cash and cash equivalents | $ 33,468 |

The carrying amount and market value of investment follows (amounts in thousands):

| | Carrying amount | Market value |
|---|---|---|
| Certificates of deposit | $ 757 | 757 |
| Common stock | 10 | 85 |
| Mortgage notes | 9 | 9 |
| Real estate held for sale | 182 | 182 |
| United States Treasury Notes | 21,377 | 21,316 |
| | $ 22,335 | 22,349 |

All investments were held in custody by the University or a commercial bank in the University's name.

**Fixed Assets**

Fixed assets are as follows (amounts in thousands):

| | |
|---|---|
| Land | $ 17,774 |
| Buildings | 202,584 |
| Site improvements | 12,352 |
| Equipment, including library books | 136,708 |
| Construction in progress | 27,946 |
| | $ 397,364 |

**Bonds Payable**

The University has issued University system revenue bonds, the proceeds of which have been used mainly to cancel and refinance previous debts incurred and finance new activities in connection with its educational facilities construction program. The following is the outstanding balance (amounts in thousands):

| Series | Principal | Annual interest rate (%) | Due date |
|---|---|---|---|
| A- Serial | $ 1,540 | 2-3/4 | 1978 - 1998 |
| B- Serial | 136 | 3-1/8 | 1978 - 2000 |
| C- Serial | 2,649 | 3 | 1978 - 2011 |
| D- Serial | 3,298 | 3-3/4 | 1978 - 2011 |
| E- Serial | 525 | 6-1/2 - 6-3/4 | 1978 - 1991 |
| E- Term | 26,000 | 7 | 2011 |
| F- Serial | 975 | 4-9/10 - 5-1/2 | 1978 - 1992 |
| F- Term | 22,000 | 5-1/2 | 2012 |
| G- Serial | 13,275 | 6-1/2 - 8 | 1978 - 2013 |
| J- Serial | 8,565 | 7 - 7-2/3 | 1994 - 2001 |
| J- Term | 17,215 | 6-1/2 - 7-3/4 | 2007 and 2013 |
| K- Serial | 31,270 | 6-1/2 - 7-3/5 | 1989 - 2000 |
| K- Term | 19,960 | 6-1/2 | 2004 |
| L- Serial | 12,715 | 6-1/2 - 7-2/3 | 1989 - 2001 |
| L- Term | 44,545 | 6-1/2 - 7-3/4 | 2007 and 2013 |
| | 204,668 | | |
| Less bond discount | 13,349 | | |
| | $ 191,319 | | |

In prior years, the University defeased certain revenue bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the university's financial statements. At year end, $43 million of revenue bonds outstanding are considered defeased.

The bonds payable require future payments of principal and interest, as follows (amounts in thousands):

| | Principal | Interest | Total |
|---|---|---|---|
| First year | $ 4,603 | 13,032 | 17,635 |
| Second year | 4,888 | 12,749 | 17,637 |
| Third year | 5,204 | 12,440 | 17,644 |
| Fourth year | 6,459 | 12,102 | 18,561 |
| Fifth year | 6,924 | 11,674 | 18,598 |
| Thereafter | 176,590 | 115,343 | 291,933 |
| Total | $ 204,668 | 177,340 | 382,008 |

These bonds are a general obligation of the University and are secured by the pledge of, and a first charge on, all revenues derived or to be derived by the University, except for appropriations and contributions, as defined in the Trust Agreement governing the bonds issued. In the event that the pledged revenues are insufficient to pay the principal of, and the interest on, the bonds, the University agrees to provide any additional required monies from other funds available to the University for such purposes, including funds appropriated by the Legislature of Puerto Rico. The revenues pledged for the year amounted to $51.4 million.

**Notes Payable**

Notes payable consist of the following (amounts in thousands):

| | |
|---|---|
| Line of credit with the Government Development Bank. Monthly interest is variable and was 7.7% | $ 6,553 |
| Promissory note due to a commercial bank payable in semiannual installments of $182 including interest | 1,525 |
| Notes payable to the U.S. Department of Education for funds used in granting long-term student loans | 185 |
| Total notes payable | $ 8,263 |

**University of Puerto Rico Retirement System - Plan Description**

The University contributes to the University of Puerto Rico Retirement System (System), a single-employer public employee retirement system that acts as a common investment and administrative agent for the University. The University payroll for employees covered by the System for the year was $205.8 million.

All full-time employees and employees contracted for a period of 9 months by the University are eligible to participate in the System. Benefits vest after 10 years of service. University employees who retire at or after age 58 with 10 years of credited service are entitled to an annual retirement benefit, payable monthly for life, in an amount equal to 1.5% of their average compensation for the highest 36 months. Maximum benefits equal to 75 percent of average compensation generally requires 30 years of service and attainment of age 55. The System also provides death and disability benefits. These benefit provisions and all other requirements are established by law.

University employees are required to contribute 4% to 7% of their annual salary to the System. The University is required to contribute 10% of applicable payroll. Effective July 1, 1990, the contribution was increased to 12%.

**Funding Status and Progress**

The amount shown below as the pension benefit obligation is a standarized disclosure measure of the present value of pension benefits, adjusted for the effect of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure is intended to help users assess the funding status of the System on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among employers. The measure is the actuarial present value of credited projected benefits, and is independent of the funding method used to determine contributions to the System.

The pension benefit obligation was computed as part of an actuarial valuation performed as of June 30, 1989. Significant actuarial assumptions used in the valuation include (a) a rate of return on the investment of present and future assets of 7.5% a year compounded annually, (b) projected salary increases of 5% a year compounded annually, attributable to inflation, (c) mortality rates based on UP-1984 Group Annuity Mortality Table, and (d) fixed retirement ages based on age at hire.

Total unfunded pension benefit obligation applicable to the University's employees at June 30, 1989 (latest actuarial valuation) follows (amounts in thousands):

| | |
|---|---|
| Pension benefit obligation: | |
| Retirees, beneficiaries and terminated employees not yet receiving benefits | $ 283,271 |
| Current employees: | |
| Accumulated employee contributions including allocated investment earnings | 78,881 |
| Employer-financed vested | 142,712 |
| Employer-financed nonvested | 42,253 |
| Total pension benefit obligation | 547,117 |
| Net assets available for benefits, at market value | 223,561 |
| Unfunded pension benefit obligation | $ 323,556 |

Several changes have occurred since the above valuation. The System granted an increase of $50 per month to each retiree receiving a pension benefit. In addition, on November 30, 1989, the Council on Higher Education allowed certain participants to change their benefit and eligibility conditions for retirement. The maximum annual compensation for those participants who had not completed 20 years of service by July 1, 1979 was raised to $31,500.

**Actuarially Determined Contribution Requirements and Contribution Made**

The System's funding policy requires actuarially determined periodic contributions at rates that, for individual employees, increase gradually over time so that sufficient assets will be available to pay benefits when due. However, the contributions are made on a predetermined basis instead of the actuarially determined basis.

The actuarial valuation as of June 30, 1989 revealed an actuarially accrued liability of at least $590 million and an unfunded accrued liability of at least $366 million. This unfunded accrued liability would have to be funded by the University at an annual rate of at least $27 million over 40 years. To provide for normal costs and administrative expenses the University would have to fund annually an additional $2.3 million.

During the year the University contributed $22.6 million to its retirement plan and recognized such amount as expenditure. The amount of $6.7 million has not been accrued in the public university funds as required by generally accepted accounting principles. Had this amount been accrued, the expenditures in the public university funds would have increased by this amount and accrued liabilities would have increased and fund balance decreased by $144 million, which represent the cumulative nonfunded amount.

**Trend Information**

Trend information gives an indication of the progress made in accumulating sufficient assets to pay benefits when due. For the year ended June 30, 1989 (latest actuarial valuation available) assets were sufficient to fund 41% of the pension benefit obligation. Unfunded pension benefit obligation represented 157% of the annual payroll for employees covered by the System. Showing unfunded pension benefit obligation as a percentage of annual covered payroll approximately adjusts for the effects of inflation for analysis purposes.

**Commitments and Contingent Liabilities**

The University has entered into various contracts for the construction of educational facilities. The uncompleted portion of these contracts amounts to $33.4 million.

The University is defendant or co-defendant in various lawsuits resulting from the ordinary conduct of business. Based on the advice from legal counsel and considering insurance coverage, management is of the opinion that the ultimate liability in excess of amounts provided, if any, will not have a significant effect on the financial position of the University.

**Subsequent Event**

In October 1991, the Government Development Bank increased $16 million to the line of credit for capital improvements.

(16) Segment Information - Proprietary Funds

Proprietary funds are primarily composed of public corporations and executive agencies which generally follow the accrual basis of accounting.

Public corporations are legally separate entities that are not operating departments of the Commonwealth. The public corporations are managed independently, outside the appropriated budget process, and their powers are generally vested in a governing board. Public corporations are established for a variety of purposes for the benefit of the Commonwealth's people such as economic development, financing and public transportation. They are not subject to Commonwealth restriction on the incurrence of debt, which apply to the Commonwealth itself, and may issue bonds and notes within legislatively authorized amounts.

The Governor of Puerto Rico, with the approval of the Senate, appoints most members of the Governing Board of most public corporations and either the Governor or the Board selects the Chief Executive Officer. Public corporations generally submit annual reports to the Governor and Legislature on their operations. Public corporations also submit to the Governor and Legislature annual budget information on operations and capital improvements (construction). The Comptroller of Puerto Rico is empowered to conduct financial and operational audits of these public corporations.

Public corporations are generally supported by revenues derived from their activities, although in recent years the Commonwealth has provided special financial assistance, in some cases of a recurring nature, to certain corporations for operating and other expenses and in fulfillment of its commitments on appropriation debt (see note 9). Financial assistance in the form of appropriated loans, contributed capital or operating subsidies for certain public corporations was provided in the year ended June 30, 1991 and such assistance is expected to be incurred in future years.

The amounts presented in the accompanying general purpose financial statements for proprietary funds include the following entities for the fiscal years indicated:

| Enterprise Funds | Year-end |
|---|---|
| Agricultural Development Administration | June 30, 1991 |
| Agricultural Services Administration | June 30, 1990 |
| Automobile Accident Compensation Administration | June 30, 1990 |
| Commercial and Agricultural Credit and Development Corporation of Puerto Rico | June 30, 1991 |
| Cooperative Development Company of Puerto Rico | June 30, 1988 |
| Corporation for Technological Transformation | June 30, 1991 |
| Corporation of Stock and Deposit Insurance for the Savings and Loans Cooperatives | June 30, 1991 |
| Economic Development Bank for Puerto Rico | June 30, 1991 |
| Farm Credit Guarantee Fund | June 30, 1991 |
| Farm Credit Trust Fund | June 30, 1991 |
| Farm Insurance Corporation | June 30, 1990 |
| Fine Arts Center Corporation | June 30, 1991 |
| Guarantee Loan Fund for Eligible Businesses | June 30, 1991 |
| Health Facilities and Services Administration of Puerto Rico | June 30, 1989 |
| Industries for the Blind, for Mentally Retarded and Other Disabled Persons of Puerto Rico | June 30, 1991 |
| Irrigation Systems of Puerto Rico | June 30, 1991 |
| Metropolitan Bus Authority | June 30, 1991 |
| Musical Arts Corporation and Subsidiaries | June 30, 1991 |
| Puerto Rico and Caribbean Cardiovascular Center Corporation | June 30, 1991 |
| Puerto Rico Aqueduct and Sewer Authority | June 30, 1991 |
| Puerto Rico Electric Power Authority | June 30, 1991 |
| Puerto Rico Housing Bank and Finance Agency (Enterprise Fund only) | June 30, 1991 |
| Puerto Rico Industrial Development Company and Subsidiaries | June 30, 1991 |
| Puerto Rico Industrial, Medical, Educational and Environmental Pollution Control Facilities Financing Authority | June 30, 1991 |

| | |
|---|---|
| Puerto Rico Land Authority | June 30, 1990 |
| Puerto Rico Maritime Shipping Authority | July 1, 1991 |
| Puerto Rico Medical Services Administration | June 30, 1991 |
| Puerto Rico Municipal Finance Agency | June 30, 1991 |
| Puerto Rico Ports Authority | June 30, 1991 |
| Puerto Rico Public Broadcasting Corporation | December 31, 1990 |
| Puerto Rico Telephone Authority and Subsidiaries | December 31, 1990 |
| Puerto Rico Urban Renewal and Housing Corporation (Enterprise Fund only) | June 30, 1990 |
| Solid Waste Authority of Puerto Rico | June 30, 1991 |
| State Insurance Fund | June 30, 1990 |
| Sugar Corporation of Puerto Rico | December 31, 1990 |
| Tourism Company of Puerto Rico (Enterprise Fund only) | June 30, 1991 |
| <u>Internal Service Funds</u> | |
| General Services Administration | June 30, 1991 |
| Government Development Bank for Puerto Rico and Subsidiaries | June 30, 1991 |
| Prison Industries Corporation | June 30, 1991 |
| Public Buildings Authority | June 30, 1991 |
| Puerto Rico Land Administration | June 30, 1990 |
| Special Fund for Loans to Governmental Entities | June 30, 1991 |

Financial Information - Enterprise Funds

Substantially all of the financial information was derived from the most recently audited financial statements and summarized into the following format. Eleven of the entities presented comprise 90% of the combined assets and of the combined operating revenues (before adjustments). The remaining portion of this note contains financial information of these entities (segment information) along with an explanation of significant and/or unusual accounting and reporting matters (amounts in thousands):

| Assets | Puerto Rico Electric Power Authority | Puerto Rico Aqueduct and Sewer Authority | Puerto Rico Urban Renewal and Housing Corporation (Unaudited) | Puerto Rico Telephone Authority | State Insurance Fund | Puerto Rico Industrial Development Company | Economic Development Bank for Puerto Rico | Puerto Rico Ports Authority | Sugar Corporation of Puerto Rico | Health Facilities and Services Administration of Puerto Rico (Unaudited) | Puerto Rico Maritime Shipping Authority | Other Entities | Total | Adjustments | Total Enterprise Funds |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Cash, cash equivalents and investments | $ 14,485 | 30,455 | 17,724 | 28,391 | 976 | 4,694 | 364,544 | 31,504 | 273 | 27,888 | 3,285 | 232,848 | 757,067 | - | 757,067 |
| Cash, cash equivalents and investments in governmental banks | - | 3,047 | - | 6,370 | 891,632 | 9,147 | 236,111 | 1,124 | 28,470 | 199 | 405 | 98,747 | 1,275,252 | - | 1,275,252 |
| Receivables, net: | | | | | | | | | | | | | | | |
| Federal Government | - | - | 248 | - | - | - | - | - | - | 17,240 | - | 2,418 | 19,906 | - | 19,906 |
| Accounts | 288,048 | 105,143 | 10,010 | 139,931 | 28,988 | 11,781 | - | 39,177 | 15,057 | 52,924 | 29,238 | 90,611 | 810,908 | - | 810,908 |
| Loans and advances | - | - | 89,709 | - | - | - | 21,035 | - | - | - | - | 83,873 | 194,617 | - | 194,617 |
| Accrued interest | 4,119 | - | 4,171 | - | 6,088 | - | 3,352 | 414 | - | - | - | 11,914 | 30,058 | - | 30,058 |
| Other | 10,969 | - | 181 | - | 3,111 | - | - | - | 442 | 1,291 | 6,667 | 15,807 | 38,468 | - | 38,468 |
| Due from other funds | 129,989 | 3,193 | 27,561 | - | 2,850 | - | - | - | 250,000 | 14,071 | - | 11,531 | 439,195 | (250,000) | 189,195 |
| Inventories | 160,855 | 16,278 | 4,161 | 62,705 | 2,290 | - | - | 2,046 | 16,377 | 17,372 | 4,977 | 35,486 | 322,547 | - | 322,547 |
| Restricted assets | 373,697 | 68,668 | 74,255 | 169,534 | - | 40,488 | 16,266 | 48,192 | 572 | 175,450 | - | 479,008 | 1,446,130 | - | 1,446,130 |
| Fixed assets, net | 2,140,363 | 2,521,610 | 1,190,137 | 1,456,552 | 12,752 | 497,014 | 345 | 357,373 | 48,676 | 124,413 | 141,281 | 346,085 | 8,836,601 | (86,349) | 8,750,252 |
| Other assets | 193,178 | 20,846 | 36,661 | 32,825 | - | 149,941 | 1,067 | 11,279 | 6,982 | 1,296 | 9,698 | 30,013 | 493,786 | - | 493,786 |
| Total assets | $ 3,315,703 | 2,769,240 | 1,454,818 | 1,896,308 | 948,687 | 713,065 | 642,720 | 491,109 | 366,849 | 432,144 | 195,551 | 1,438,341 | 14,664,535 | (336,349) | 14,328,186 |
| Liabilities | | | | | | | | | | | | | | | |
| Accounts payable and accrued liabilities | 304,291 | 142,243 | 53,558 | 186,904 | 624,271 | 19,688 | 7,197 | 29,130 | 10,291 | 118,759 | 74,045 | 288,514 | 1,858,891 | - | 1,858,891 |
| Deposits | - | - | - | - | - | - | 427,212 | - | - | | - | - | 427,212 | - | 427,212 |
| Due to other funds | - | - | 12,988 | - | - | - | - | - | 60 | - | - | 3,442 | 16,490 | - | 16,490 |
| Securities sold under agreements to repurchase | - | - | - | - | - | - | 121,502 | - | - | - | - | - | 121,502 | - | 121,502 |
| Interest payable | 73,838 | 22,452 | 73,191 | 4,063 | - | 6,214 | 2,419 | 4,015 | - | 2,568 | 501 | 22,485 | 211,746 | - | 211,746 |
| Deferred revenue | - | - | - | - | 19,091 | - | - | - | - | 1,384 | - | 13,128 | 33,603 | - | 33,603 |
| Notes payable | 233,500 | 169,255 | 533,217 | 141,005 | - | 51,958 | 24,000 | 4,402 | 290,000 | 429,154 | 287,256 | 297,691 | 2,461,438 | (250,000) | 2,211,438 |
| Bonds payable | 2,291,140 | 454,818 | 563,253 | 938,527 | - | 160,812 | - | 149,269 | - | - | - | 382,642 | 4,940,461 | - | 4,940,461 |
| Accrued compensated absences | 113,401 | 37,269 | - | 27,572 | 10,737 | 4,592 | 730 | 7,368 | 977 | 41,627 | 1,181 | 14,329 | 259,783 | - | 259,783 |
| Other long-term liabilities | - | - | - | 33,426 | - | - | - | 1,284 | 6,695 | 112,070 | 40,497 | 4,771 | 198,743 | (112,070) | 86,673 |
| Total liabilities | 3,016,170 | 826,037 | 1,236,207 | 1,331,497 | 654,099 | 243,264 | 583,060 | 195,468 | 308,023 | 705,562 | 403,480 | 1,027,002 | 10,529,869 | (362,070) | 10,167,799 |
| Fund Equity/(Deficit) | | | | | | | | | | | | | | | |
| Contributed capital | 120,714 | 1,811,903 | 1,244,612 | 4,962 | - | 291,205 | 43,991 | 174,149 | 166,728 | - | 97,614 | 469,476 | 4,425,354 | - | 4,425,354 |
| Retained earnings/(deficit) | 178,819 | 131,300 | (1,026,001) | 559,849 | 294,588 | 178,596 | 15,669 | 121,492 | (107,902) | (273,418) | (305,543) | (58,137) | (290,688) | 25,721 | (264,967) |
| Total fund equity/(deficit) | 299,533 | 1,943,203 | 218,611 | 564,811 | 294,588 | 469,801 | 59,660 | 295,641 | 58,826 | (273,418) | (207,929) | 411,339 | 4,134,666 | 25,721 | 4,160,387 |
| Total liabilities and fund equity | $ 3,315,703 | 2,769,240 | 1,454,818 | 1,896,308 | 948,687 | 713,065 | 642,720 | 491,109 | 366,849 | 432,144 | 195,551 | 1,438,341 | 14,664,535 | (336,349) | 14,328,186 |

| Operations | Puerto Rico Electric Power Authority | Puerto Rico Aqueduct and Sewer Authority | Puerto Rico Urban Renewal and Housing Corporation (Unaudited) | Puerto Rico Telephone Authority | State Insurance Fund | Puerto Rico Industrial Development Company | Economic Development Bank for Puerto Rico | Puerto Rico Ports Authority | Sugar Corporation of Puerto Rico | Health Facilities and Services Administration of Puerto Rico (Unaudited) | Puerto Rico Maritime Shipping Authority | Other Entities | Total | Adjustments | Total Enterprise Funds |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Operating revenues: | | | | | | | | | | | | | | | |
| Charges for services | $ 1,263,397 | 283,549 | 33,602 | 699,103 | 275,664 | 50,864 | - | 88,129 | 54,434 | 110,203 | 309,788 | 294,883 | 3,463,616 | - | 3,463,616 |
| Financing income | - | - | 11,981 | - | - | - | 2,272 | - | - | - | - | 5,806 | 20,059 | - | 20,059 |
| Investment earnings | - | - | - | - | - | - | 46,329 | - | - | - | - | 46,810 | 93,139 | - | 93,139 |
| Other | - | - | - | - | 2,138 | 2,864 | 5,197 | - | - | 6,560 | 50,860 | 19,000 | 86,619 | - | 86,619 |
| Total operating revenues | 1,263,397 | 283,549 | 45,583 | 699,103 | 277,802 | 53,728 | 53,798 | 88,129 | 54,434 | 116,763 | 360,648 | 366,499 | 3,663,433 | - | 3,663,433 |
| Operating expenses: | | | | | | | | | | | | | | | |
| Cost of services | 925,166 | 263,506 | 69,187 | 399,138 | 366,720 | 19,726 | 7,074 | 80,283 | 90,614 | 652,573 | 315,038 | 443,324 | 3,632,349 | 36,071 | 3,668,420 |
| Interest | - | - | 38,747 | - | - | - | 37,451 | - | - | - | - | 36,787 | 112,985 | - | 112,985 |
| Depreciation and amortization | 106,014 | 50,072 | 2,634 | 145,117 | 1,159 | 11,598 | 182 | 13,840 | 3,086 | 10,247 | 19,234 | 13,647 | 376,830 | (6,636) | 370,194 |
| Other | - | - | - | - | - | - | 5,148 | - | - | - | - | 2,832 | 7,980 | 124 | 8,104 |
| Total operating expenses | 1,031,180 | 313,578 | 110,568 | 544,255 | 367,879 | 31,324 | 49,855 | 94,123 | 93,700 | 662,820 | 334,272 | 496,590 | 4,130,144 | 29,559 | 4,159,703 |
| Operating income/(loss) | 232,217 | (30,029) | (64,985) | 154,848 | (90,077) | 22,404 | 3,943 | (5,994) | (39,266) | (546,057) | 26,376 | (130,091) | (466,711) | (29,559) | (496,270) |
| Non-operating revenues/(expenses): | | | | | | | | | | | | | | | |
| Federal subsidies and grants | - | - | 39,163 | - | - | - | - | - | - | 96,611 | - | 9,731 | 145,505 | - | 145,505 |
| Interest income | 33,953 | 9,437 | - | 19,288 | 65,269 | 5,400 | - | 6,764 | - | 4,174 | - | 22,054 | 166,339 | - | 166,339 |
| Interest expense | (163,069) | (24,313) | - | (88,086) | - | (13,409) | - | (5,388) | (35,332) | (19,983) | (23,321) | (8,480) | (381,381) | 44,675 | (336,706) |
| Other, net | (93,015) | (4,673) | (510) | (25,305) | - | (6,488) | - | (167) | 4,018 | - | 343 | 26,016 | (99,781) | - | (99,781) |
| Total non-operating revenues/ (expenses), net | (222,131) | (19,549) | 38,653 | (94,103) | 65,269 | (14,497) | - | 1,209 | (31,314) | 80,802 | (22,978) | 49,321 | (169,318) | 44,675 | (124,643) |
| Income/(loss) before operating transfers and extraordinary gain | 10,086 | (49,578) | (26,332) | 60,745 | (24,808) | 7,907 | 3,943 | (4,785) | (70,580) | (465,255) | 3,398 | (80,770) | (636,029) | 15,116 | (620,913) |
| Operating transfers in | - | 28,558 | 33,566 | - | - | - | - | - | 58,213 | 393,867 | - | 130,928 | 645,132 | (36,738) | 608,394 |
| Operating transfers out | - | - | - | - | (10,116) | - | - | - | - | - | - | (31,588) | (41,704) | - | (41,704) |
| Operating transfers, net | - | 28,558 | 33,566 | - | (10,116) | - | - | - | 58,213 | 393,867 | - | 99,340 | 603,428 | (36,738) | 566,690 |
| Income/(loss) before extraordinary gain | 10,086 | (21,020) | 7,234 | 60,745 | (34,924) | 7,907 | 3,943 | (4,785) | (12,367) | (71,388) | 3,398 | 18,570 | (32,601) | (21,622) | (54,223) |
| Extraordinary gain | - | - | - | - | - | - | - | - | - | - | - | 14,418 | 14,418 | - | 14,418 |
| Net income/(loss) | 10,086 | (21,020) | 7,234 | 60,745 | (34,924) | 7,907 | 3,943 | (4,785) | (12,367) | (71,388) | 3,398 | 32,988 | (18,183) | (21,622) | (39,805) |
| Retained earnings/(deficit) at beginning of year: | | | | | | | | | | | | | | | |
| As previously reported | 168,733 | 167,050 | (1,033,235) | 499,104 | 329,512 | 170,689 | 11,726 | 132,105 | (95,535) | (202,030) | (308,941) | (97,001) | (257,823) | 93,699 | (164,124) |
| Restatements | - | (14,730) | - | - | - | - | - | (3,362) | - | - | - | 5,076 | (13,016) | - | (13,016) |
| As restated | 168,733 | 152,320 | (1,033,235) | 499,104 | 329,512 | 170,689 | 11,726 | 128,743 | (95,535) | (202,030) | (308,941) | (91,925) | (270,839) | 93,699 | (177,140) |
| Contributions | - | - | - | - | - | - | - | - | - | - | - | 3,140 | 3,140 | 29,644 | 32,784 |
| Transfers from/(to) contributed capital | - | - | - | - | - | - | - | (2,466) | - | - | - | 25,463 | 22,997 | - | 22,997 |
| Residual equity transfer out | - | - | - | - | - | - | - | - | - | - | - | - | - | (76,000) | (76,000) |
| Effect of inclusion of prior year operations | - | - | - | - | - | - | - | - | - | - | - | (27,803) | (27,803) | - | (27,803) |
| Retained earnings/(deficit) at end of year | $ 178,819 | 131,300 | (1,026,001) | 559,849 | 294,588 | 178,596 | 15,669 | 121,492 | (107,902) | (273,418) | (305,543) | (58,137) | (290,688) | 25,721 | (264,967) |

The following paragraphs summarize significant information related to the entities for which summarized financial information is included in this note:

**Puerto Rico Electric Power Authority**

Puerto Rico Electric Power Authority (PREPA) is a public corporation created in 1941 for the purpose of conserving, developing and utilizing the water and power resources of Puerto Rico. PREPA produces, transmits and distributes substantially all of the electric power consumed in Puerto Rico.

Due from other funds as of June 30, 1991 includes $94.9 million related to fuel adjustment subsidies granted to certain residential customers and $35 million for reimbursements of certain costs incurred by the irrigation systems administered by PREPA.

In October 1991, PREPA entered into an agreement with the Commonwealth for the repayment of the fuel adjustment subsidy receivable as of June 30, 1991. Under this agreement, the Commonwealth will pay this amount over a fifteen-year period commencing with the 1993 fiscal year in installments of approximately $6.3 million per year without interest. The reimbursements of the costs incurred on behalf of the irrigation systems will be reduced against the required contribution of in lieu of taxes due by PREPA to the Commonwealth.

In February 1991, PREPA amended the regulations related to fuel adjustment subsidies to eliminate the subsidy to residential customers other than public housing residents, lifeline customers, university students, the elderly and handicapped.

Restricted assets consist of cash, cash equivalents and investments held for debt service, construction and other specific operating purposes.

Fixed assets consist mainly of utility plant. Cost includes indirect charges for engineering, supervision, transportation and an allowance for the cost of funds used during construction.

PREPA's construction program for the next year amounts to $288 million.

PREPA is required to make contributions in lieu of taxes as defined in the law. Such contribution for the year amounted to $93 million and is presented as other non-operating expense.

Notes payable consist mainly of $120 million to Government Development Bank and commercial banks for the financing of fuel purchases and capital improvements and $108 million of bond anticipation notes, which were paid with the proceeds of a subsequent bond issuance.

Bonds payable consist of $687 million of electric bonds and $1.68 billion of power revenue bonds, which are presented net of bond discounts of $76 million. These bonds were issued for financing the cost of capital improvements.

PREPA defeased certain revenue bonds in prior years by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the defeased bonds. Accordingly, the trust assets and the liabilities for the defeased bonds are not included in PREPA's financial statements. Bonds outstanding as of June 30, 1991 and considered defeased amount to $512.3 million.

PREPA has a pension plan covering substantially all its employees which is administered by the Employees Retirement System of the Puerto Rico Electric Power Authority (the System). Employees are required to contribute approximately 9% of their salary and PREPA is required to contribute the remaining amounts necessary to fund the System, using the projected benefit method. The pension expense for the year was $45 million. The total unfunded pension and related benefit obligation was $319.7 million at June 30, 1991.

PREPA also provides certain health care benefits for retired employees and spouses based on a cost plus plan. The cost of health care benefits to retirees amounted to $12.5 million during the year.

PREPA is obligated, pursuant to Commonwealth and United States government requirements, to incur capital improvements and undertake maintenance programs necessary to comply with environmental regulations in the areas of waste and air pollution control, noise abatement and control of certain toxic substances. PREPA estimates its expenditures for these programs to approximate $95.5 million during the next five years.

Subsequent to June 30, 1991 PREPA issued $250 million Power Revenue Bonds, Series P, to repay Bond Anticipation Notes under a $115 million line of credit and to finance a portion of the costs of various capital improvement projects. The interest rate of these bonds ranges from 5.20% to 7% with maturities through year 2021.

**Puerto Rico Aqueduct and Sewer Authority**

Puerto Rico Aqueduct and Sewer Authority (PRASA) was created as a public corporation in 1945 for the purpose of owning, operating and developing all of the public water supplies and sewer systems in Puerto Rico.

Restricted assets consist of cash, cash equivalents and investments held mainly for debt service.

PRASA's fixed assets consist principally of aqueduct and sewer facilities. Cost includes labor, materials, administrative costs and interest expense on debt-financed construction.

Bonds payable consist of revenue bonds and includes $61.5 million whose debt service is reimbursed by the Commonwealth. Upon payment by the Commonwealth, PRASA records the reimbursed amount as contributed capital.

PRASA has defeased certain revenue bonds by placing the proceeds of new bonds and of revenue bonds issued by the Puerto Rico Infrastructure Financing Authority in irrevocable trusts to provide for all future debt service payments on the defeased bonds. Accordingly, the trust assets and the liabilities for the defeased bonds are not included in PRASA's financial statements. Bonds outstanding at June 30, 1991 and considered defeased amount to $555.6 million.

Notes payable include $163.2 million due to the Government Development Bank in accordance with loan agreements under which PRASA can borrow up to $175 million for the purpose of providing interim financing for construction projects. The amount of $100 million is due July 1, 1992 and is expected to be paid from the proceeds of future revenue bond issues. The amount of $63.2 million is due under an agreement with maximum borrowing of $75 million due from December 1991 through December 2004. The Puerto Rico Infrastructure Finance Authority (PRIFA) has agreed to make all principal and interest payments under this agreement from federal excise taxes or other Commonwealth's appropriations received by PRIFA after payment of PRIFA debts.

Facilities and operations of PRASA are subject to regulation under numerous Federal and Commonwealth environmental laws, including the Federal Clean Water Act (the Act), administered by the Environmental Protection Agency (EPA). In January 1978, the United States, acting on behalf of EPA, initiated litigation against PRASA and the Commonwealth to enforce compliance with the Act, with respect to violations of the Act occurring at numerous plants in PRASA's sewer system.

In 1988, PRASA and EPA entered into an agreement to settle and resolve all the outstanding claims. As a result, PRASA paid $2 million to the United States Treasury in settlement of all outstanding claims; deposited $7.9 million into a fund to be used for a number of management and planning projects required to be conducted; amended requirements and schedules for plant improvements; and adopted an implementation schedule for the industrial pretreatment program.

PRASA estimates that the capital cost of complying with the terms of this agreement will be $92.4 million through June 30, 1994. Such amount is expected to be derived from a combination of internally generated funds, appropriations to be made by the Commonwealth, Federal Government grants and loans and future revenue bonds.

The Commonwealth reimburses PRASA for all operating, maintenance and depreciation expenses incurred in excess of revenues for the operations in rural areas. The reimbursement for the year was $28.5 million and is presented as operating transfers in.

During the year ended June 30, 1991, PRASA recorded adjustments to beginning retained earnings amounting to $14.7 million representing accounting errors in the computation of subsidy reimbursements by the Commonwealth from 1976 to 1982.

Subsequent to June 30, 1991, PRASA issued serial bonds amounting to $8.4 million to provide funds for its capital improvements and to refinance notes payable amounting to $6 million.

**Puerto Rico Urban Renewal and Housing Corporation (Unaudited)**

Puerto Rico Urban Renewal and Housing Corporation (PRURHC) is a public corporation created in 1957 to, among other things, acquire, lease and operate certain housing projects; provide for the construction, improvement, alteration or repair of such housing projects, and accept mortgages as security for the payment of land and dwellings sold by PRURHC. As of July 1, 1990, the activities of PRURHC related to public housing were transferred to a new agency (Public Housing Administration). Subsequent to June 30, 1991 certain assets and liabilities were transferred to the Puerto Rico Department of Housing. For the remaining assets and liabilities the Governor of Puerto Rico approved a law to liquidate PRURHC and create the Office for the Liquidation of the Accounts of the Puerto Rico Urban Renewal and Housing Corporation (the Office), to carry out the liquidation process. The Office is being administered by a Trustee appointed by the Governor of Puerto Rico. Such trustee is responsible for obtaining the maximum realization from the sale of PRURHC assets (mainly fixed assets) to third parties, in order to meet most of PRURHC's obligations with it own resources. The Trustee assumed control of PRURHC assets, legal rights, claims and obligations, liabilities, equity, all records and documents. No authorization is provided to the Trustee, to commit for the repayment of debts from the general fund of the Commonwealth, unless previously authorized by the Legislature. All bonds issued and outstanding that have been guaranteed by the Commonwealth will continue to have such guarantee.

The carrying value of the assets and liabilities transferred to the Department of Housing and to the Office has not been determined. Also, the fixed assets available for sale have not been determined, therefore, they cannot be adjusted to reflect their net realizable value. Accordingly, no provision for any loss that may result has been made in the accompanying general purpose financial statements.

The accounting policies followed by PRURHC in its federally-assisted programs, presented as enterprise funds, are those prescribed by the U.S. Department of Housing and Urban Development. Also, certain of these policies are followed by other funds.

The funds of PRURHC included as enterprise consist of the operations of the Housing Administration Fund, Low Cost Housing Fund and Federally-assisted Titles I and III.

Mortgage notes receivable (included in loan and advances) of $106 million and housing units held for sale (included in other assets) of $64 million are presented net of allowance for losses of $40 million and $36 million, respectively.

Notes receivable (included in loan and advances) includes $23 million from the Puerto Rico Housing Bank and Finance Agency.

Restricted assets consist of cash, cash equivalents and investments.

Fixed assets consist mainly of low cost condominiums, housing facilities and construction in progress and were substantially financed with U.S. Federal contributions. No depreciation was provided on fixed assets and it was not possible to determine the amount of such depreciation.

Notes payable include $450.6 million issued to finance the construction and management of certain low-cost housing facilities. These notes are substantially repaid with U.S. Federal Government contributions.

Bonds payable amounting to $338 million include $106.7 million which are guaranteed by the Commonwealth as to principal and interest for an amount not to exceed $325 million and $231.3 million which are being paid from Commonwealth appropriations. Bonds payable of $226 million are paid from annual contributions received from the Federal Government and are secured by housing units. These bonds are presented in the combined balance sheet net of a bond discount of $1 million.

**Puerto Rico Telephone Authority**

Puerto Rico Telephone Authority (PRTA) was created as a public corporation in 1974 for the purpose of acquiring, developing and operating telephone, telegraph, radio, cable or other communication systems.

The consolidated financial statements of PRTA include the accounts of its wholly-owned subsidiaries, Puerto Rico Telephone Company (PRTC), Telefónica Larga Distancia (TLD) and Puerto Rico Communications Corporation (PRCC), formerly Puerto Rico Communications Authority (PRCA). All significant intercompany transactions and balances were eliminated in the consolidation except those attributable to and involved with regulated operations. PRTA has majority ownership in a joint venture, which investment is not significant, and is accounted for using the equity method of accounting. PRTC provides local and long distance telephone service within Puerto Rico. TLD provides overseas long distance telecommunications service. PRCC provides local and long-distance telephone services to certain areas not serviced by PRTC.

On May 30, 1990 PRTA acquired the net assets of PRCA for a payment of $76 million to the general fund of the Commonwealth, and the assumption of $19.9 million related to a possible liability to the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities. PRTA received net assets of $100.8 million, which exceeded the purchase price by $4.9 million and such excess was recorded as contributed capital. The payment was recorded as a residual equity transfer in the general purpose financial statements of the Commonwealth for the year ended June 30, 1990, since such payment was received by the general fund during such year. However, since the payment is recorded in the PRTA financial statements included herein, it is adjusted and reflected as a residual equity transfer out in the enterprise fund.

Restricted assets consist of cash, cash equivalents and investments, including $91.6 million of interest bearing deposits in governmental banks. Such assets are mainly held for debt service, construction and other specific operating purposes.

Fixed assets consist mainly of the telephone plant and equipment. Cost includes indirect cost (payroll taxes and other fringe benefits) and interest charged during construction.

The construction program for the next year amounts to $242.4 million, including commitments for the purchase and installation of telephone equipment and materials.

On August 3, 1989, PRTA issued subordinated notes for the amount of $25.1 million to be payable in the next ten-year period. The proceeds were used to acquire the Company's distribution and purchasing center and circuits of the American Telephone and Telegraph fiber optic cable from Florida to Puerto Rico. PRTA entered into an interest rate swap agreement on the variable interest rate subordinate notes amounting to $14.7 million. As a result of the agreement, the effective rate was 6.85% during the year. The interest rate on the remaining $10.4 million ranges from 6.60% to 6.85%.

Bonds payable consist of senior revenue bonds and sinking fund debentures issued to finance the construction of communication facilities.

PRTA and its wholly-owned subsidiaries are exempt from all taxes levied on their properties or revenues by the Commonwealth and its municipalities. However, the law requires payments in lieu of taxes determined on the basis of PRTA's annual net revenues as defined therein. During the year, PRTA's provision for the payment of in lieu of taxes amounted to $21.1 million and is presented as other non-operating expense.

PRTC has two separate non-contributory defined benefits pension plans covering substantially all its salaried and hourly employees. The funding policy for these plans is to make the annual contributions as required by applicable regulations. The pension expense for the year was $9.3 million.

During September 1991, PRTA was granted an increase of $47 million in the line of credit with GDB. This line of credit will be used to finance the capital improvements program for the following year. The line of credit is due on June 30, 1992 and will be paid from the proceeds of a future bond issuance and from other available funds.

A law was approved in July 1991 that requires from PRTA, commencing in April 1992, a payment in lieu of taxes to the Secretary of the Treasury of not less than $20 million or the equivalent of 4% of gross revenues of PRTA and its subsidiaries as determined by the Board of Directors. This payment will be used for educational purposes by the Department of Education or the Office for the Improvement of the Puerto Rico Public Schools.

Subsequent to June 30, 1991, PRTA entered into an agreement to sell 80% of the ownership of TLD for $141.6 million. Such agreement is subject to the approval of the Federal Communications Commission.

The proceeds of the sale will be deposited with PRTA and used to meet certain financial obligations to bondholders. The remaining proceeds, estimated at $100 million, will be contributed to the Commonwealth's education fund.

**State Insurance Fund**

State Insurance Fund (SIF) was created as an executive agency in 1935 to provide workers' compensation and disability benefit insurance to employees who suffer accidents during the course or as consequence of functions which are inherent to their work.

Cash in governmental banks consists primarily of short-term interest bearing deposits in the Government Development Bank. Accrued liabilities include $599 million of accruals for losses and loss adjustment expenses based on actuarial studies.

Accounts receivable consist of premiums net of a reserve for doubtful accounts of $74 million. The report of the other auditors on the financial statements of SIF indicates that the internal controls and accounting records are not adequate to ascertain that all premiums are recorded. The auditors' opinion on such financial statements was qualified for the effect of such adjustments, if any, which would have been necessary to premiums income and receivables if such controls and records were adequate.

During August 1991 the Legislature created the Workers Welfare Security Occupational and Health Fund, and SIF transferred $65 million to such fund. The purpose of the fund is to improve the workers well-being through programs, housing projects, rehabilitation and prevention of illnesses and accidents.

**Puerto Rico Industrial Development Company**

Puerto Rico Industrial Development Company (PRIDCO) was created as a public corporation in 1942 primarily to stimulate the formation of new local enterprises and to encourage mainland United States and foreign enterprises to establish operations in Puerto Rico. To accomplish its mission, PRIDCO constructs industrial facilities for lease or sale to qualified enterprises. PRIDCO also owns several tourism properties, of which some are managed and operated by third parties under rental contracts. Under the Special Incentives Program, PRIDCO administers disbursements of legislative appropriations to manufacturers, in reimbursement of allowable start-up costs.

The consolidated financial statements of PRIDCO include its wholly-owned subsidiaries except for certain wholly-owned subsidiaries engaged in tourist operations which are accounted for on the equity basis since PRIDCO is attempting to dispose of them. No loss is expected on this disposition.

Fixed assets consist mainly of industrial and tourism properties. For the year ending June 30, 1992, PRIDCO estimates expenditures amounting to $78.6 million for construction, land acquisition and development.

Restricted assets consist mainly of time deposits and U.S. government securities in sinking funds accounts. Other assets include $103.3 million of land held for improvement or sale.

Notes payable include loans of $18 million from commercial banks to finance the construction of its office buildings and future rental facilities. These notes are secured by mortgages on land and by assignment of rents under lease agreements.

Bonds payable consist of revenue refunding and general purpose revenue bonds. These bonds are being paid through rental and management contract revenues received from industrial and tourist properties rented to third parties.

During October 1991, PRIDCO issued $70 million Revenue Bonds and $84.7 million Refunding Revenue Bonds. The proceeds of such bonds were used to provide funds for the payment of $43.4 million of notes, for additional capital improvements and to advance refund $78.3 million of Revenue Bonds. The new bonds are payable from gross revenues received by PRIDCO from certain of its properties, and if required, from other available funds.

During November 1991, PRIDCO created Hotel Development Corporation (HDC) as a subsidiary to assist hotel developers in the public and private sector. PRIDCO will transfer all of its hotels with a carrying value of $250 million to HDC.

**Economic Development Bank for Puerto Rico**

Economic Development Bank for Puerto Rico (EDB) was created as a public corporation in 1985 for the promotion of the development of the private sector of the economy of the Commonwealth.

Cash, cash equivalents and investments include interest-bearing deposits with other banks amounting to $224.2 million; securities purchased under agreements to resell amounting to $123.5 million; bank acceptances amounting to $14.9 million; and other investments amounting to $1.9 million.

Under a regulation issued by the Commonwealth's Commissioner of Financial Institutions, all financial institutions receiving eligible funds as defined and commonly known as "936 funds" are required to invest 1% through September 30, 1989 and 1.6% thereafter of the average balance of such eligible funds in deposits, loans or obligations of EDB. As of June 30, 1991, EDB had time deposits and securities sold under agreements to repurchase, received under the provision of said Regulation amounting to $121.1 million. Also, to comply with other investment requirements of said Regulation, eligible institutions had time deposits and securities sold under agreements to repurchase amounting to $198.6 million at June 30, 1991.

In 1987, the Legislature of the Commonwealth approved an increase of $35 million in EDB's capital. EDB has received legislative appropriations amounting to $27 million of these funds through June 30, 1991 and will receive $8 million in the year ending June 30, 1992.

In August 1990 the Commercial and Agricultural Credit and Development Corporation was created and ascribed to EDB to promote the agricultural and commercial development of Puerto Rico. This corporation received the assets and liabilities of the Farm Credit Corporation and the Commercial Development Company of Puerto Rico, both component units of the Commonwealth of Puerto Rico. This corporation provides, among other things, loans to the commercial and agricultural sectors. Its business is administered and its corporate powers are executed by a Board of Directors and a management group common to that of EDB.

**Puerto Rico Ports Authority**

Puerto Rico Ports Authority (PRPA) was created as a public corporation in 1942 to administer all ports and aviation transportation facilities of the Commonwealth and to render other related services.

Restricted assets consist mainly of cash, cash equivalents and investments, including $7.4 million of interest-bearing deposits in the Government Development Bank. Such assets are held for debt service, construction, maintenance and other specific operating purposes.

Fixed assets consist primarily of land, buildings and piers.

Bonds payable consist of serial and term revenue bonds amounting to $156 million. These bonds are presented in the balance sheet net of bond discount of $6.7 million. All revenues derived from PRPA's properties, as defined, are pledged to secure the revenue bonds payable.

During the year ended June 30, 1991, PRPA recorded adjustments to beginning retained earnings amounting to $3.4 million representing mainly fringe benefits obligations incurred in prior years which were not recorded at June 30, 1990.

**Sugar Corporation of Puerto Rico**

Sugar Corporation of Puerto Rico (SCPR), a related entity of the Puerto Rico Land Authority, was organized as a public corporation in 1973 to consolidate the Commonwealth's activities in the sugar industry. SCPR is engaged in the production of raw and refined sugar in Puerto Rico and buys all the cane produced by private growers.

SCPR depends on subsidies from the Commonwealth of Puerto Rico to provide the necessary funds to cover its cash deficits. During the year, SCPR received $58.2 million in such subsidies. The portion relating to the operating loss is recorded as a reduction of the loss and the portion identifiable with acquisition of assets or payment of bonds principal is recorded as contributed capital.

Notes payable and other long-term liabilities include $250 million and $2.4 million, respectively, of debt to be paid from future legislative appropriations. SCPR has established a receivable for the $250 million appropriation which is presented as due from other funds. The receivable and debt were eliminated through an adjustment and the debt is presented in the Commonwealth's general long-term debt account group.

SCPR is a defendant in various legal actions. Aggregate claims under these actions amount to approximately $62.6 millions. SCPR is in the process of litigating these actions, and has recorded a reserve for possible losses of $4.3 million; however, the ultimate outcome of the actions cannot presently be determined and it is not presently known whether this reserve will be sufficient to provide for possible losses the SCPR may sustain as a result of the final outcome of such claims.

**Health Facilities and Services Administration of Puerto Rico (Unaudited)**

Health Facilities and Services Administration of Puerto Rico (HFSA) was created as an executive agency in 1975 to lease and operate hospitals and other health facilities and to provide for the improvement, alteration or repair of such facilities. HFSA is authorized to borrow money and issue notes or other obligations for the purpose of financing the costs of improvements and providing health services to the general public. Patients admitted to an institution under the jurisdiction of HFSA who are indigent receive hospital and medical services free of charge; otherwise payments for services rendered are required.

Notes payable mainly consist of $425 million from Government Development Bank to refinance an existing loan. These notes are general obligations of HFSA and are secured by Medicaid payments.

Other long-term liabilities consist of capital leases with the Public Buildings Authority related to property and equipment with a carrying value of $86.3 million. As the leases are with a public authority which is part of the Commonwealth's reporting entity, the criteria for recording as a capital lease do not apply in the general purpose financial statements of the Commonwealth as the asset and debt should only be reported by the Public Buildings Authority and not by HFSA. Accordingly, an adjustment was made to eliminate the liability, interest, asset and depreciation of HFSA from the enterprise fund and account for the related lease as operating.

**Puerto Rico Maritime Shipping Authority**

Puerto Rico Maritime Shipping Authority (PRMSA) is a public corporation created in 1974 for the purpose of establishing and maintaining an economical maritime transportation system between Puerto Rico and abroad.

PRMSA has not been able to finance its operations solely through internally generated funds. Extensive financial support has been provided by the Commonwealth, principally through the Government Development Bank for Puerto Rico, in the form of extensions of credit, direct loans, loan guarantees and capital contributions. The Commonwealth approved a law in 1988 to contribute $10 million each year from 1989 to 1994 to help guarantee the operational and functional stability of operations.

Fixed assets consist mainly of vessels, containers and terminal property.

Notes payable includes $148.6 million due to the Government Development Bank for Puerto Rico (GDB); $56.9 million guaranteed by GDB and $60 million guaranteed by the full faith, credit and taxing power of the Commonwealth. The amount of $8.6 million of the debt to GDB will be paid by future legislative appropriations.

Other long-term liabilities consist mainly of the present value of obligation under capital leases for vessels.

## Other Information - Enterprise Funds

### Cash, Cash Equivalents and Investments

Public corporations invest primarily in U.S. government and agency securities and bankers acceptances. Public corporations may invest in those securities authorized by legal provisions set forth in their Organic Act and/or provisions set forth in Bond Trust Indentures.

As of June 30, 1991, the carrying value of cash and cash equivalents amounts to $453.3 million and the bank balance to $536.3 million. This bank balance consists of $309.5 million which is insured or collateralized with securities held by the Department of the Treasury and $226.8 million which is uninsured and uncollateralized. In addition, cash in Government Development Bank and Economic Development Bank with a carrying value and a bank balance of $1 billion is not insured or collateralized.

Cash and cash equivalents included in restricted assets had a carrying value of $389.8 million and bank balance of $382.7 million. This bank balance consists of $144 million which is insured or collateralized with securities held by the Department of the Treasury and $238.7 million which is not insured or collateralized.

The following table shows the carrying amount and market value (amounts in thousands) as of June 30, 1991 of investments of all entities included within the enterprise funds. Investments are categorized below to give an indication of the level of risk at June 30, 1991. Category 1 includes investments that are insured or collaterized with securities maintained by the Secretary of the Treasury in his name. Category 2 includes investments that are collaterized with securities maintained by financial institutions or their agents in the name of the public corporation. Category 3 includes investments that are uncollaterized.

| | Carrying Amount | | | | Market |
|---|---|---|---|---|---|
| | Category 1 | Category 2 | Category 3 | Total | Value |
| **Unrestricted** | | | | | |
| U.S. Government and agencies | $ 70,205 | - | 65 | 70,270 | 69,890 |
| Corporate stocks & bonds | - | 87,619 | 1,049 | 88,668 | 93,559 |
| Mortgage loans | 1,249 | - | - | 1,249 | 1,249 |
| Certificates of deposit and bankers' acceptances | 5,219 | 920 | 252,453 | 258,592 | 258,642 |
| Others | 81,250 | 34,577 | - | 115,827 | 115,827 |
| | $ 157,923 | 123,116 | 253,567 | 534,606 | 539,167 |
| Investment held by broker-dealers relating to securities and loans sold under agreements to repurchase | | | | 21,652 | 21,596 |
| | | | | $ 556,258 | 560,763 |
| **Restricted** | | | | | |
| U.S. Government Securities | $ 95,968 | 445,100 | - | 541,068 | 542,134 |
| P.R. Municipal bonds | 122,780 | - | - | 122,780 | 122,780 |
| Certificates of deposit and bankers' acceptances | 75,788 | 72,676 | 104,408 | 252,872 | 252,872 |
| Guaranteed Investment contracts | - | 27,462 | - | 27,462 | 27,462 |
| Others | 16,266 | - | - | 16,266 | 16,266 |
| | $ 310,802 | 545,238 | 104,408 | 960,448 | 961,514 |

Restricted assets (before adjustments) of all significant entities, amounting to $1.4 billion as of June 30, 1991 primarily consist of $1.3 billion of cash, cash equivalents and investments held for the redemption of bonds and notes payables.

**Fixed Assets**

Changes in fixed assets of all entities included in the enterprise funds were as follows (amounts in thousands):

| | Balance Beginning of Year | Additions | Retirements | Balance End of Year |
|---|---|---|---|---|
| Puerto Rico Electric Power Authority | $ 3,152,858 | 268,643 | 11,387 | 3,410,114 |
| Puerto Rico Aqueduct and Sewer Authority | 2,771,493 | 176,014 | - | 2,947,507 |
| Puerto Rico Urban Renewal and Housing Corporation (Unaudited) | 1,349,839 | - | 132,895 | 1,216,944 |
| Puerto Rico Telephone Authority* | 2,023,440 | 243,950 | 90,279 | 2,177,111 |
| State Insurance Fund | 22,090 | 1,446 | - | 23,536 |
| Puerto Rico Industrial Development Company | 637,903 | 86,949 | 58,436 | 666,416 |
| Economic Development Bank for Puerto Rico | 736 | 137 | 7 | 866 |
| Puerto Rico Ports Authority | 469,946 | 42,107 | 933 | 511,120 |
| Sugar Corporation of Puerto Rico | 103,568 | 1,125 | 8,770 | 95,923 |
| Health Facilities and Services Administration of Puerto Rico (Unaudited) | 56,101 | 12,282 | 2,696 | 65,687 |
| Puerto Rico Maritime Shipping Authority | 310,611 | 14,276 | 8,526 | 316,361 |
| Other | 418,794 | 59,067 | 10,733 | 467,128 |
| | $ 11,317,379 | 905,996 | 324,662 | 11,898,713 |
| Less accumulated depreciation and amortization | | | | 3,148,461 |
| | | | | $ 8,750,252 |

*includes the fixed assets of the Puerto Rico Communications Authority.

Fixed assets at June 30, 1991 are comprised of the following (amounts in thousands):

| | |
|---|---|
| Land and improvements | $ 315,678 |
| Buildings and improvements | 7,081,635 |
| Equipment | 3,299,722 |
| Construction in progress | 1,201,678 |
| | $ 11,898,713 |

**Bonds Payable**

Certain public corporations issued their own serial, revenue and refunding bonds. These bonds, which have interest rates ranging from 2.125% to 12%, are not legal obligations of the Commonwealth. Changes in bonds outstanding of all entities were as follows (amounts in thousands):

| Issuer | Outstanding Beginning of Year | Issued | Redeemed | Outstanding End of Year |
|---|---|---|---|---|
| Puerto Rico Electric Power Authority | $ 2,332,363 | 15,153 | 56,376 | 2,291,140 |
| Puerto Rico Aqueduct and Sewer Authority | 461,793 | - | 6,975 | 454,818 |
| Puerto Rico Urban Renewal and Housing Corporation (Unaudited) | 586,160 | - | 22,907 | 563,253 |
| Puerto Rico Telephone Authority* | 962,144 | - | 23,617 | 938,527 |
| Puerto Rico Industrial Development Company | 169,427 | - | 8,615 | 160,812 |
| Puerto Rico Ports Authority | 116,083 | 81,899 | 48,713 | 149,269 |
| Other | 409,328 | - | 26,686 | 382,642 |
| Total | $ 5,037,298 | 97,052 | 193,889 | 4,940,461 |

*includes the bonds payable of the Puerto Rico Communications Authority.

Amounts due to maturity are as follows (amounts in thousands):

| | |
|---|---|
| First year | $ 225,804 |
| Second year | 185,339 |
| Third year | 189,659 |
| Fourth year | 223,868 |
| Fifth year | 197,836 |
| Thereafter | 3,917,955 |
| | $ 4,940,461 |

**Notes Payable**

Notes payable were issued by certain public corporations to provide interim financing for special projects or financing of operations. Interest rates range from 4.5% to 12%. Changes in notes payable for all entities were as follows (amounts in thousands):

| Issuer | Outstanding Beginning of Year | Issued | Redeemed | Outstanding End of Year |
|---|---|---|---|---|
| Puerto Rico Electric Power Authority | $ 170,000 | 118,500 | 55,000 | 233,500 |
| Puerto Rico Aqueduct and Sewer Authority | 125,019 | 52,868 | 8,632 | 169,255 |
| Puerto Rico Urban Renewal and Housing Corporation (Unaudited) | 654,678 | - | 121,461 | 533,217 |
| Puerto Rico Telephone Authority* | 69,745 | 76,000 | 4,740 | 141,005 |
| Puerto Rico Industrial Development Company | 22,478 | 33,512 | 4,032 | 51,958 |
| Economic Development Bank for Puerto Rico | 24,000 | - | - | 24,000 |
| Puerto Rico Ports Authority | 4,695 | 201 | 494 | 4,402 |
| Sugar Corporation of Puerto Rico | 40,000 | 40,000 | 40,000 | 40,000 |
| Health Facilities and Services Administration (Unaudited) | 91,428 | 350,000 | 12,274 | 429,154 |
| Puerto Rico Maritime Shipping Authority | 294,455 | 42,851 | 50,050 | 287,256 |
| Other | 271,220 | 61,050 | 34,579 | 297,691 |
| Total | $ 1,767,718 | 774,982 | 331,262 | 2,211,438 |

*includes the notes payable of the Puerto Rico Communications Authority.

Amounts due to maturity (except for the Puerto Rico Urban Renewal and Housing Corporation for which the information is not available) are as follows (amounts in thousands):

| | |
|---|---|
| First year | $ 579,063 |
| Second year | 183,475 |
| Third year | 106,886 |
| Fourth year | 46,372 |
| Fifth year | 80,686 |
| Thereafter | 681,739 |
| | $ 1,678,221 |

Puerto Rico Industrial, Medical, Educational and Environmental Pollution Control Facilities Financing Authority, a component unit, has issued revenue bonds of which $2 billion are outstanding at June 30, 1991. The bonds are payable solely from and secured by a pledge and assignments of amounts payable under loan agreements.

They are also unconditionally guaranteed by the borrowers, their parent company and/or letters of credit from banks. These bonds do not constitute a debt or a pledge of the full faith and credit of the Authority or the Commonwealth and are not reflected as a liability in these general purpose financial statements.

**Leases**

Public corporations are also committed under numerous operating leases. Rental expense under these agreements amounted to $73.5 million. Future minimum lease payments under noncancellable leases exceeding one year for all entities are as follows (amounts in thousands):

| | |
|---|---|
| First year | $ 39,930 |
| Second year | 32,804 |
| Third year | 28,810 |
| Fourth year | 23,263 |
| Fifth year | 16,199 |
| Thereafter | 61,370 |
| Total future minimum lease payments | $ 202,376 |

**Individual Deficits**

Component units included under other entities and with a fund deficit include Farm Credit Guarantee Fund administered by Commercial and Agricultural Credit and Development Corporation ($47.6 million), Puerto Rico Land Authority ($10.7 million), and Musical Arts Corporation and Subsidiaries ($2 million).

**Other Contingencies**

Puerto Rico Land Authority and Commercial Agricultural Credit and Development Corporation of Puerto Rico are defendant under various legal proceedings arising in the normal course of business. Aggregate claims under these cases amount to $192 million. Management believes, based on the opinion of legal counsel, that the final disposition of these matters will not have a material adverse effect on the financial position or results of operations.

**Contributed Capital**

Changes in contributed capital for the year ended June 30, 1991 are summarized as follows (amounts in thousands):

| | |
|---|---|
| Contributed capital at beginning of year | $ 4,353,705 |
| Transfers from/(to) retained earnings, net | (22,997) |
| Net contributions | 94,646 |
| Contributed capital at end of year | $ 4,425,354 |

**Extraordinary Gain**

During February 1991, the Metropolitan Bus Authority (MBA) transferred to the Employee's Retirement System of the Government of Puerto Rico (ERS) a real property with a carrying value of $259 thousands, in settlement of a liability with the ERS of $14.7 million. The difference of $14.4 million between the liability and the carrying value was recognized as an extraordinary gain.

**Subsequent Event**

The Puerto Rico Housing Bank and Finance Agency issued Special Obligations Refunding Bonds (Series H) amounting to $91.8 million, to provide funds to refund all the outstanding special obligation bonds of the Puerto Rico Urban Renewal and Housing Corporation, which was dissolved effective August 9, 1991. The Bonds are secured by the pledge of the Commonwealth of Puerto Rico to draw from any available funds in the Treasury of Puerto Rico to cover for any required amount needed for the payment of principal and interest of such bonds in an aggregate principal amount not exceeding $325 million. The good faith and credit of the Commonwealth of Puerto Rico are pledged to such payments.

**Financial Information - Internal Service Funds**

Substantially all of the financial information was derived from the most recently audited financial statements and summarized into the following format. Two of the entities presented comprise 96% of the combined assets and 94% of the combined operating revenues (before adjustments). This note contains financial information of these entities (segment information) along with an explanation of significant and/or unusual accounting and reporting matters (amounts in thousands).

COMMONWEALTH OF PUERTO RICO

Notes to General Purpose Financial Statements

| | Government Development Bank for Puerto Rico | Public Buildings Authority | Other Entities | Total | Adjustments | Total Internal Service Funds |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash, cash equivalents and investments | $ 3,262,290 | 17,307 | 83 | 3,279,680 | - | 3,279,680 |
| Cash, cash equivalents and investments in governmental banks | - | 64,176 | 24,101 | 88,277 | - | 88,277 |
| Receivables, net: | | | | | | |
| Accounts | - | 19,703 | 8,751 | 28,454 | - | 28,454 |
| Loans and advances | 1,570,063 | - | 37,503 | 1,607,566 | - | 1,607,566 |
| Accrued interest | 88,155 | - | 2,665 | 90,820 | - | 90,820 |
| Other | - | 12,054 | 10,838 | 22,892 | - | 22,892 |
| Due from other funds | - | 35,080 | - | 35,080 | - | 35,080 |
| Inventories | - | - | 160,890 | 160,890 | - | 160,890 |
| Restricted assets | 1,877,881 | 144,446 | 6,132 | 2,028,459 | - | 2,028,459 |
| Fixed assets, net | - | 1,169,094 | 62,679 | 1,231,773 | (291,890) | 939,883 |
| Other assets | 70,061 | 4,990 | 1,003 | 76,054 | - | 76,054 |
| Total assets | $ 6,868,450 | 1,466,850 | 314,645 | 8,649,945 | (291,890) | 8,358,055 |
| **Liabilities** | | | | | | |
| Accounts payable and accrued liabilities | 39,169 | 53,696 | 41,940 | 134,805 | - | 134,805 |
| Deposits | 4,282,464 | - | - | 4,282,464 | - | 4,282,464 |
| Due to other funds | 7,519 | 31,870 | 20,545 | 59,934 | - | 59,934 |
| Securities sold under agreements to repurchase | 468,337 | - | - | 468,337 | - | 468,337 |
| Interest payable | 65,513 | 35,180 | 6,224 | 106,917 | - | 106,917 |
| Notes payable | 230,954 | 34,148 | 59,986 | 325,088 | - | 325,088 |
| Bonds payable | 1,108,334 | 965,330 | - | 2,073,664 | - | 2,073,664 |
| Accrued compensated absences | 3,473 | 7,477 | 5,003 | 15,953 | - | 15,953 |
| Other long-term liabilities | - | - | 1,389 | 1,389 | - | 1,389 |
| Total liabilities | 6,205,763 | 1,127,701 | 135,087 | 7,468,551 | - | 7,468,551 |
| **Fund Equity** | | | | | | |
| Contributed capital | 650,000 | 41,230 | 92,035 | 783,265 | - | 783,265 |
| Retained earnings | 12,687 | 297,919 | 87,523 | 398,129 | (291,890) | 106,239 |
| Total fund equity | 662,687 | 339,149 | 179,558 | 1,181,394 | (291,890) | 889,504 |
| Total liabilities and fund equity | $ 6,868,450 | 1,466,850 | 314,645 | 8,649,945 | (291,890) | 8,358,055 |

| Operations | Government Development Bank for Puerto Rico | Public Buildings Authority | Other Entities | Total | Adjustments | Total Internal Service Funds |
|---|---|---|---|---|---|---|
| Operating revenues: | | | | | | |
| Charges for services | $ 45,308 | 150,198 | 41,337 | 236,843 | (8,351) | 228,492 |
| Financing income | 133,602 | - | 2,183 | 135,785 | - | 135,785 |
| Investment earnings | 351,279 | - | - | 351,279 | - | 351,279 |
| Other | - | - | 3,542 | 3,542 | - | 3,542 |
| Total operating revenues | 530,189 | 150,198 | 47,062 | 727,449 | (8,351) | 719,098 |
| Operating expenses: | | | | | | |
| Cost of services | 41,509 | 54,755 | 43,326 | 139,590 | - | 139,590 |
| Interest | 385,313 | 66,915 | 1,995 | 454,223 | - | 454,223 |
| Depreciation and amortization | - | - | 1,255 | 1,255 | 29,662 | 30,917 |
| Other | 13,406 | - | 1,513 | 14,919 | - | 14,919 |
| Total operating expenses | 440,228 | 121,670 | 48,089 | 609,987 | 29,662 | 639,649 |
| Operating income/(loss) | 89,961 | 28,528 | (1,027) | 117,462 | (38,013) | 79,449 |
| Non-operating revenues/(expenses): | | | | | | |
| Interest income | - | 25,000 | 36 | 25,036 | - | 25,036 |
| Interest expense | - | - | (23) | (23) | - | (23) |
| Other, net | - | (80,920) | 8 | (80,912) | 82,728 | 1,816 |
| Total non-operating revenues, net | - | (55,920) | 21 | (55,899) | 82,728 | 26,829 |
| Income/(loss) before operating transfers | 89,961 | (27,392) | (1,006) | 61,563 | 44,715 | 106,278 |
| Operating transfers in | - | - | 3,000 | 3,000 | - | 3,000 |
| Net income/(loss) | 89,961 | (27,392) | 1,994 | 64,563 | 44,715 | 109,278 |
| Retained earnings at beginning of year | 52,726 | 325,311 | 44,945 | 422,982 | (336,605) | 86,377 |
| Transfers to contributed capital | (130,000) | - | - | (130,000) | - | (130,000) |
| Residual equity transfer in | - | - | 40,584 | 40,584 | - | 40,584 |
| Retained earnings at end of year | $ 12,687 | 297,919 | 87,523 | 398,129 | (291,890) | 106,239 |

The following paragraphs summarize significant information related to the entities for which summarized financial information is included in this note:

**Government Development Bank for Puerto Rico**

Government Development Bank for Puerto Rico (GDB) was created as a public corporation in 1948 to act as fiscal agent for the Commonwealth and its public entities and to make loans to public entities and private enterprises which will further the economic development of Puerto Rico.

Legislation has been enacted authorizing the Director of the Office of Budget and Management and the Secretary of the Treasury of the Commonwealth to include in future Commonwealth budget appropriations funds to support certain public entities in repaying their loans and advances. At June 30, 1991 loans and advances amounting to $491.8 million were being paid under these provisions.

As of June 30, 1991, the book balance of cash equivalents amounted to $2.3 billion and of cash in bank to $8.6 million. The bank balance of cash in bank amounted to $8.4 million. Of this balance $7.7 million are uninsured and uncollateralized and the remainder is covered by federal depository insurance. Cash equivalents consist of $1.1 billion of federal funds sold and $1.2 billion of certificates of deposit and bankers acceptances. Of this balance $122 million is insured and collateralized, the remainder is uninsured and uncollateralized. Investments are categorized below to give an indication of the level of risk at June 30, 1991. Category 1 includes investments that are insured or registered or for which the securities are held by GDB or its agent in GDB's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in GDB's name (amounts in thousands).

| Investments | Category 1 | Category 2 | Carrying Amount | Market Value |
|---|---|---|---|---|
| U.S. Government Securities | $ 48,862 | - | 48,862 | 48,782 |
| Commonwealth securities | 4,285 | - | 4,285 | 4,347 |
| Mortgages obligations | 217,646 | - | 217,646 | 217,178 |
| Certificates of deposits and banker's acceptance | - | 666,126 | 666,126 | 666,126 |
| | $ 270,793 | 666,126 | 936,919 | 936,433 |

| Restricted Assets | Category 1 | Category 2 | Carrying Amount | Market Value |
|---|---|---|---|---|
| Treasury investment growth receipts | $ 306,617 | - | 306,617 | 406,836 |
| Certificates of deposit | - | 311,130 | 311,130 | 311,130 |
| Mortgage loans | 60,249 | - | 60,249 | 59,034 |
| U.S. and Commonwealth securities | 420,106 | - | 420,106 | 424,533 |
| Guaranteed investment contract | - | 333,948 | 333,948 | 333,948 |
| | $ 786,972 | 645,078 | 1,432,050 | 1,535,481 |
| Investment held by broker-dealers relating to securities and loans sold under repurchase agreements | | | 445,831 | 450,450 |
| | | | $ 1,877,881 | 1,985,931 |

Deposits consist mainly of interest bearing deposits of $2.1 billion and certificates of deposit of $2.1 billion principally from the Commonwealth and its public corporations.

Securities sold under agreements to repurchase of $468.3 million consist of federal funds amounting to $8 million and securities and loans sold under agreements to repurchase representing borrowings with maturities ranging from one day to six months. As of June 30, 1991, the amount outstanding and interest rates for securities and loans sold under agreements to repurchase were as follows (amounts in thousands):

| | |
|---|---|
| Amount outstanding at end of year | $ 460,337 |
| Maximum amount outstanding at any month-end | $ 474,606 |
| Average amount outstanding | $ 316,383 |
| Weighted average interest rate for the year | 6.96% |
| Weighted average interest rate at June 30, 1991 | 5.89% |

The market value of the securities and loans underlying the repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in such market value. As of June 30, 1991, the market value of the underlying securities and loans plus accrued interest exceeded the Bank's obligation, including accrued interest, by approximately $2.1 million.

Bonds payable of $317 million are guaranteed by the Commonwealth as to payments of principal and interest for an amount not to exceed $550 million. These bonds include $50 million secured by a letter of credit issued by a commercial bank. The remaining $267 million represent adjustable refunding bonds due January 1, 2015, and secured by letters of credit issued by commercial banks. The letters of credit will expire on February 28, 1995, or earlier upon the conversion of the bonds to a fixed rate of interest.

Bonds payable of $450 million bear interest of 10%. Interest and principal payments are secured by letters of credit issued by commercial banks and by Treasury Investment Growth Receipts (TIGR's) with a carrying value of $306.6 million at June 30, 1991 and held by GDB as restricted assets. Such TIGR's represent evidence of ownership of future interest and principal payments aggregating $1.4 billion in U.S. Treasury Bonds, 12%, maturing through August 15, 2013. The TIGR's are pledged to secure each interest and principal payment from August 15, 1994 to 2013 on the bonds and have maturity dates and face amounts coinciding with such due dates and amounts.

Interest rates on notes and bonds range from 6.25% to 10% on $747.7 million, are variable on $469.8 million and $133.5 million were issued with a discount as zero coupon. Changes in bonds and notes outstanding were as follows (amounts in thousands):

| | Outstanding Beginning of Year | Issued | Redeemed | Outstanding End of Year |
|---|---|---|---|---|
| Notes | $ 215,500 | 229,873 | 214,419 | 230,954 |
| Bonds | 804,445 | 340,859 | 25,155 | 1,120,149 |
| | 1,019,945 | 570,732 | 239,574 | 1,351,103 |
| Less discount | 10,065 | | | 11,815 |
| Total | $ 1,009,880 | | | 1,339,288 |

A summary of notes and bonds payable, which mature during the next years, follows (amounts in thousands):

| Year ending June 30 | Amount |
|---|---|
| 1992 | $ 120,604 |
| 1993 | 25,000 |
| 1994 | 10,500 |
| 1995 | 80,500 |
| 1996 | 31,400 |
| Thereafter | 1,083,099 |
| | $ 1,351,103 |

GDB is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit and to purchase participations, standby letters of credit and financial guarantees, and interest rate products. These instruments involve, to varying degrees, elements of credits and interest rate risk that are not recognized in the balance sheet.

The off-balance sheet risk is managed and monitored in manners similar to those used for on-balance sheet risk. GDB exposure to credit loss for lending commitments and letter of credit is represented by the contractual amount of those transactions. Since many of the commitments are expected to expire without being drawn upon, the total amount does not necessarily represent future cash receipts. The notional amounts for other off-balance sheet risk express the dollar volume of the transactions, but the credit risk is much smaller. At June 30, 1991, financial instruments whose contract amounts represents credit risk consists of (amounts in thousands):

| | |
|---|---|
| Financial guarantees | $ 111,768 |
| Standby letters of credit | 181,574 |
| Commitments to purchase participations | 56,111 |
| Commitments to extend credit | 323,838 |

Also, financial instruments whose notional amount exceeds the amount of credit risk at June 30, 1991, consist of $321.3 million interest rate swap agreements.

At June 30, 1991, GDB guarantees obligations issued by public entities, amounting to $349.4 million. Also it has undisbursed loan commitments of $23.8 million to the private sector and of $300 million to public entities.

GDB has entered into various interest rate swap agreements with certain financial institutions for an aggregate notional principal amount of $321.3 million. GDB pays, based on the floating three-month London interbank offered rate (LIBOR), on a notional principal amount of $165.5 million while the financial institutions pay fixed rates ranging from 7.88% to 9.53%. GDB pays fixed rates ranging from 6.98% to 9.15% on a notional principal amount of $155.8 million while the financial institutions pay based on LIBOR. Under these agreements the net interest amounts are paid semiannually.

At June 30, 1991, assets held in trust by GDB in its fiduciary capacity and not included in GDB's consolidated financial statements amounted to $703.8 million.

**Public Buildings Authority**

Public Buildings Authority (PBA) was created as a public corporation in 1958 to design and construct office buildings, courts, warehouses and related facilities for lease to the Commonwealth of Puerto Rico or any of its departments, agencies, instrumentalities or municipalities and to finance and construct schools, health-care and social welfare facilities.

The annual rent for each building leased is computed based on the amounts needed by PBA for: (1) principal, interest and other amortization requirements of the notes and bonds issued to finance the buildings; (2) operating and maintenance expenses of the buildings, including a reasonable proportional share of PBA's administrative expenses, excluding depreciation; (3) cost of equipment replacement and other noncurrent operating and maintenance costs; and (4) reserve for such purposes. Rentals for operating and maintenance expenses, together with equipment replacement, are subject to escalation to permit PBA to recover costs in these areas.

The full faith, credit and taxing power of the Commonwealth are pledged for the payment of the rentals under any lease agreement executed pursuant to the law that created PBA. The law also provides that the Commonwealth's Department of the Treasury will make advances to PBA for any unpaid portion of rentals payable to PBA by any agency or instrumentality of the Commonwealth under the lease agreements.

During the year ended June 30, 1990 it was determined that PBA would credit to the general fund approximately $94 million for debt service rentals. This credit arises from Supplemental Bonds Resolutions adopted by PBA to permit substitutions of funds deposited in bond reserve accounts, with letters of credit and bond insurance policies, and to withdraw the moneys and securities on deposits in such accounts. As a result, $86 million were deposited in Bonds Resolution Debt Services Account. PBA in an agreement with the Department of the Treasury of the Commonwealth, credited the Commonwealth for $86 million, plus interest to be earned, against debt services rental payment requirements from May 1990 to August 1991. The audited financial statements of PBA recognized $82.7 million of this credit as of June 30, 1991. However, since PBA have remitted $65 million to the Commonwealth, the remaining $29 million were recognized as due to other fund. Also since the full credit was recognized as a residual equity transfer out as of June 30, 1990 in the Commonwealth's general purpose financial statements, the financial statements of PBA as of June 30, 1991 were adjusted to remove the $82.7 million credit.

Cash included in cash, cash equivalents and investments with a carrying value of $17.3 is insured or collateralized with securities held by the Department of the Treasury. Cash in governmental banks amounting to $64.1 million is not insured or collateralized.

Restricted assets consist of cash, certificates of deposit and U.S. Government obligations amounting to $74.3 million held in bond sinking funds and $70.1 million held in or related to construction funds. Cash with a carrying value of $19.2 million is insured or collateralized with securities held by the Department of the Treasury. Investments are composed of $125.2 million of U.S. Government and agencies securities. These investments are insured, registered or held by the public corporation or its agent in the public corporation's name.

Fixed assets are presented at cost and include a portion of general, administrative and interest expenses allocated during the construction period. Fixed assets with a cost of $1.03 billion are leased to government agencies under operating leases and no depreciation is computed on such assets in the audited financial statements of PBA. To conform with generally accepted accounting principles as applicable to the general purpose financial statements, an adjustment was made for an estimate of such depreciation through June 30, 1991.

Bonds payable consist of serial revenue, term revenue, serial, term and capital appreciation bonds with an outstanding balance at June 30, 1991 amounting to $989 million and are presented in the combined balance sheet net of bond discount of $23.7 million. Such bonds are due through 2017 and bear interest from 5% to 8.875%. Aggregate principal maturities in future years are as follows (amounts in thousands):

| Year ending June 30 | |
|---|---|
| 1992 | $ 24,970 |
| 1993 | 31,120 |
| 1994 | 33,060 |
| 1995 | 35,385 |
| 1996 | 37,870 |
| Thereafter | 826,637 |
| | $ 989,042 |

The maturities are funded by debt service rentals to be collected from the lessees. The payment of principal and interest on the bonds payable is guaranteed by the Commonwealth of Puerto Rico to a maximum aggregate principal amount not to exceed $1.2 billion.

In prior years, PBA defeased certain bonds with the net proceeds of new bonds which were irrevocably deposited in trusts to provide for all future debt service payments on the defeased bonds. Accordingly, the defeased bonds are no longer deemed outstanding and $422 million of bonds as of June 30, 1991 are considered defeased.

PBA has entered into various contracts with outside contractors for the construction of buildings and other facilities. The uncompleted portion of these contracts amounts to $112 million as of June 30, 1991.

During March 1992, PBA issued $210 million of bonds to finance the construction of health facilities and public schools, and $173.7 million of refunding bonds to advance refund $173.1 million outstanding bonds. The proceeds of the refunded bonds will be deposited in an escrow for investment in non-cancellable direct obligations of the United States, the principal and interest on which, with other uninvested moneys, will be sufficient to pay when due the principal of and premiums and interest on such bonds. The good faith and credit of the Commonwealth are pledged for the payment of the bonds.

**Other Information - Internal Service Funds**

Inventories included under other entities mainly consist of $159.9 million of land leased or held for future use or sale to other governmental entities by the Puerto Rico Land Administration.

## (17) Restatements

The beginning retained earnings/(deficit) in the enterprise fund have been restated mainly to give retroactive effect to accounting errors in the computation of subsidies reimbursement and unrecorded fringe benefits obligations incurred in prior years.

## (18) Subsequent Events

In August 1991 the Puerto Rico Highway and Transportation Authority entered into a line of credit agreement with the Government Development Bank for advances not to exceed $150 million and to be used for contruction activities corresponding to fiscal year 1991-1992. This line of credit will be payable in March 1992 with interest revised on a quarterly basis.

In August 1991, the Office for the Improvement of the Puerto Rico Public Schools obtained a $125 million loan from GDB. The proceeds of the loan will be used for the rehabilitation of the public schools facilities and the acquisition of educational materials and equipment. The loan will be paid beginning in 1992 by a payment in lieu of taxes, of not less than $20 million, from the PRTA Educational Excellence Fund. The loan bears interest at 8.5% and is due on May 1, 2000.

From November 1991 through February 1992, the Commonwealth collected approximately $216 million (unaudited) of taxes in arrears from individuals, corporations and partnerships as a result of a tax amnesty approved by the legislature.

In March 1992, the Commonwealth issued $64.2 million of refunding bonds to advance refund $59.8 million outstanding bonds and $305 million of public improvement bonds to finance the cost of certain public improvements. The proceeds of the refunded bonds will be deposited in an escrow for investment in non-cancellable direct obligations of the United States, the principal and interest on which, with other uninvested moneys, will be sufficient to pay when due the principal of and premium and interest on such bonds. The bonds are due on July 1, 2021 and bear interest from 5% to 6.8%. The good faith, credit and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal and interest of these bonds.

In April 1992, the Puerto Rico Highway and Transportation Authority issued $117 million Special Facility Revenue Bonds. The proceeds were loaned to a private company for the construction of the San José Lagoon Bridge Project. These bonds are payable from an assignment of revenues to be derived from the loan agreement.

In June 1992, the Puerto Rico Highway and Transportation Authority issued $425 million Highway Revenue Bonds and $186.8 million Highway Revenue Refunding Bonds. The proceeds from the revenue bonds were used to finance or refinance a portion of the costs of various projects under the Authority's Construction Program. The proceeds of the refunding bonds were deposited in an escrow for investment in obligations of the United States, the principal and interest on which, with other available monies, will be sufficient to pay when due the principal of and premium and interest on bonds amounting to $169 million. The bonds are due on July 1, 2022 and bear interest from 3.5% to 6.7%.

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# PUERTO RICO
# PUBLIC BUILDINGS AUTHORITY

## Report on Audits of Financial Statements for the years ended June 30, 1992 and 1991

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To The Board of Directors of
PUBLIC BUILDINGS AUTHORITY:

## Report of Independent Accountants

We have audited the financial statements of the various funds and financial statement schedules of the PUBLIC BUILDINGS AUTHORITY for the years ended June 30, 1992 and 1991, as listed in the foregoing table of contents. These financial statements and financial statement schedules are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and the financial statement schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial statement schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The Authority has excluded from their financial statements depreciation of its property and equipment that, in our opinion, should be expensed in order to conform with generally accepted accounting principles. If property and equipment were depreciated property and equipment and capital would have been decreased by $326,404,157 and $291,889,797, respectively, as of June 30, 1992 and 1991, and revenues would have been decreased by $34,514,360 and $31,007,319 for the years ended June 30, 1992 and 1991, respectively. Refer to Note 14 to the financial statements.

In our opinion, except for not depreciating property and equipment as discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Public Buildings Authority as of June 30, 1992 and 1991 and the results of its operations and changes in financial position of the various funds for the years ended June 30, 1992 and 1991 in conformity with generally accepted accounting principles. In addition, in our opinion, the financial statement schedules referred to above, when considered in relation to the basic financial statements taken as a whole, present fairly, in all material respects, the information required to be included therein.

In connection with our audit, nothing came to our attention that caused us to believe that the monies received by the Public Buildings Authority under Bond Resolutions No. 77 and No. 158 have not been applied in accordance with the provisions of such resolutions. However, it should be noted that our audit was not directed primarily toward obtaining knowledge of such noncompliance.

San Juan, Puerto Rico
September 25, 1992

COOPERS & LYBRAND

Stamp Number 1120685 of the
Puerto Rico Society of Certified
Public Accountants has been
affixed to the file copy of this
report.

## PUBLIC BUILDINGS AUTHORITY

### BALANCE SHEETS — ALL FUNDS

**As of June 30, 1992 and 1991**

### AUTHORITY'S FUNDS

| | 1992 | 1991 |
|---|---|---|
| **ASSETS** | | |
| CURRENT ASSETS: | | |
| Cash, including certificates of deposit of $90,166,000 in 1992 and $79,746,000 in 1991 (Note 5) | $ 158,212,737 | $ 96,151,665 |
| Rent receivables (Notes 1 and 2) | 30,046,282 | 19,703,439 |
| Other receivables | 6,615,119 | 12,054,305 |
| Prepaid expenses | 6,388,312 | 4,519,808 |
| Total current assets | 201,262,450 | 132,429,217 |
| Due from Agency Fund | 54,076,005 | 38,539,059 |
| Property and equipment (Notes 1, 3 and 14) | 1,245,795,045 | 1,169,093,520 |
| Restricted assets (Notes 4, 6 and 11) | 56,813,850 | 74,256,682 |
| Construction Funds — restricted (Note 5) | 88,463,992 | 55,519,996 |
| Other assets | 2,003,605 | 469,847 |
| | $1,648,414,947 | $1,470,308,321 |
| **LIABILITIES AND CAPITAL** | | |
| CURRENT LIABILITIES: | | |
| Note payable | $ 262,424 | $ 232,888 |
| Accounts payable | 9,627,657 | 39,206,390 |
| Accrued expenses | 11,930,248 | 13,022,219 |
| Due to contractors | 15,077,845 | 22,448,106 |
| Contract retentions | 16,824,115 | 15,782,440 |
| Total Current Liabilities | 53,722,289 | 90,692,043 |
| Due to Agency Fund (Note 15) | 4,981,899 | 3,458,870 |
| Liabilities currently payable from restricted assets (Notes 4 and 6): | | |
| Current portion of long-term debt (Notes 1, 6 and 11) | 22,240,000 | 24,956,660 |
| Interest | 35,867,140 | 35,179,712 |
| | 58,107,140 | 60,136,372 |
| Long-Term Debt (Notes 1, 6 and 11) | 1,133,049,736 | 976,872,248 |
| Commitments and contingent liabilities (Notes 9 and 10) | | |
| Capital (Notes 7, 11 and 16) | 398,553,883 | 339,148,788 |
| | $1,648,414,947 | $1,470,308,321 |

### AGENCY FUND

| | 1992 | 1991 |
|---|---|---|
| **ASSETS** | | |
| Due from Authority's Funds | $ 4,981,899 | $ 3,458,870 |
| Property and equipment: | | |
| Land | 8,029,610 | 1,705,657 |
| Construction in progress | 135,443,661 | 85,156,120 |
| | $ 148,455,170 | $ 90,320,647 |
| **LIABILITIES** | | |
| Advances from governmental agencies | $ 94,379,165 | $ 51,781,588 |
| Due to Authority's Funds | 54,076,005 | 38,539,059 |
| | $ 148,455,170 | $ 90,320,647 |

*The accompanying notes are an integral part of these financial statements.*

## STATEMENTS OF REVENUES AND EXPENSES

### AUTHORITY'S FUNDS

**For the years ended June 30, 1992 and 1991**

| | 1992 | 1991 |
|---|---|---|
| Revenues: | | |
| Rent: | | |
| Debt-service rentals | $ 106,178,799 | $ 94,278,523 |
| Operating rental | 58,601,692 | 55,919,242 |
| | 164,780,491 | 150,197,765 |
| Other, including interest income of $10,557,750 in 1992 and $25,000,000 in 1991 | 11,249,060 | 26,807,590 |
| Total revenues | 176,029,551 | 177,005,355 |
| Expenses: | | |
| Net interest and other financing expenses (Note 6) | 69,829,958 | 66,914,662 |
| Salaries and employee benefits (Note 8) | 39,472,373 | 36,079,763 |
| Utilities | 8,517,948 | 8,296,959 |
| Repairs and maintenance | 14,378,787 | 7,012,757 |
| Security services | 5,302,185 | 5,171,220 |
| Rent and insurance | 1,422,714 | 1,244,169 |
| Other expenses | 6,463,282 | 1,365,712 |
| | 145,387,247 | 126,085,242 |
| Less administrative expenses applied to construction in progress | 4,749,218 | 4,416,062 |
| Total expenses | 140,638,029 | 121,669,180 |
| Revenues in excess of expenses before extraordinary (loss), savings in debt services and reserve substitution credit | 35,391,522 | 55,336,175 |
| Savings in Debt Service (Note 16) | 29,243,577 | — |
| Reserve substitution credit (Note 12) | — | (82,727,984) |
| Extraordinary (loss) — early extinguishment of debt (Note 11) | (5,230,004) | — |
| Net revenues (loss) in excess of expenses | $ 59,405,095 | $ (27,391,809) |

*The accompanying notes are an integral part of these financial statements.*

## STATEMENTS OF CHANGES IN CAPITAL

### AUTHORITY'S FUNDS

**For the years ended June 30, 1992 and 1991**

| | Contributed Capital | Accumulated Net Revenues (Note 7) | Total |
|---|---|---|---|
| Balance at June 30, 1990 | $ 41,229,913 | $325,310,684 | $366,540,597 |
| Net revenues (loss) in excess of expenses | — | (27,391,809) | (27,391,809) |
| Balance at June 30, 1991 | 41,229,913 | 297,918,875 | 339,148,788 |
| Net revenues (loss) in excess of expenses | — | 59,405,095 | 59,405,095 |
| Balance at June 30, 1992 | $ 41,229,913 | $357,323,970 | $398,553,883 |

*The accompanying notes are an integral part of these financial statements.*

## STATEMENTS OF CASH FLOWS

### AUTHORITY'S FUNDS
**For the years ended June 30, 1992 and 1991**

| | 1992 | 1991 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net revenues (loss) in excess of expenses | $ 59,405,095 | $(27,391,809) |
| Adjustments to reconcile net revenues (loss) in excess of expenses to net cash provided by operating activities: | | |
| Amortization of bond discount | 2,655,014 | 2,376,530 |
| Accretion of bonds | 4,535,528 | 6,003,757 |
| Change in assets and liabilities: | | |
| (Increase) in rent receivables | (10,342,843) | (17,241,783) |
| (Increase) decrease in other receivables | 5,439,186 | (10,158,475) |
| (Increase) in prepaid expenses | (1,868,504) | (18,079) |
| (Increase) decrease in due from Agency Fund | (15,536,946) | 6,686,111 |
| (Decrease) in restricted assets | 17,442,832 | 61,253,836 |
| (Increase) in construction funds — restricted | (32,943,996) | 29,927,699 |
| (Increase) decrease in other assets | (1,533,758) | — |
| Increase (decrease) in interest payable | 687,428 | (2,353,074) |
| Increase (decrease) in accounts payable | (29,578,733) | 20,962,947 |
| Increase (decrease) in accrued expenses | (1,091,971) | 1,662,091 |
| Increase (decrease) in due to contractors | (7,370,261) | 8,567,314 |
| Increase (decrease) in contract retentions | 1,041,675 | (617,833) |
| Increase (decrease) in due to Agency Fund | 1,523,029 | (6,702,867) |
| Total adjustments | (66,942,320) | 100,348,174 |
| Net cash provided by (used in) operation activities | (7,537,225) | 72,956,365 |
| Cash flows from investing activities: | | |
| Capital expenditures, net | (76,701,525) | (79,648,379) |
| Net cash used in investing activities | (76,701,525) | (79,648,379) |
| Cash flows from financing activities: | | |
| Net borrowings (payments) under line of credit agreement | (34,148,174) | 23,147,777 |
| Principal payments on notes | (236,969) | (266,406) |
| Proceeds from issuance of long-term debt | 378,706,278 | — |
| Repayment of long-term debt | (198,021,313) | (23,877,866) |
| Net cash provided by (used in) financing activities | 146,299,822 | (996,495) |
| Net increase (decrease) in cash | 62,061,072 | (7,688,509) |
| Cash at beginning of year | 96,151,665 | 103,840,174 |
| Cash at end of year | $158,212,737 | $ 96,151,665 |
| Supplemental Disclosure of Cash Flow Information: | | |
| Cash paid during the year for: | | |
| Interest | $ 69,142,530 | $ 68,411,072 |

Supplemental Schedule of non-cash financing activities:

The Authority eliminated from its accounts credits related to savings in debt service from a defeasance of bonds. This transaction resulted in rent receivables and capital increasing by $29,243,577 respectively.

*The accompanying notes are an integral part of these financial statements.*

## NOTES TO FINANCIAL STATEMENTS

### NOTE 1 — ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES

#### Organization

The Public Buildings Authority (the Authority), a corporate body and politic of the Commonwealth of Puerto Rico (the Commonwealth) exercising public and governmental functions, was created on June 19, 1958 by Act No. 56 of the Legislature of Puerto Rico (The Enabling Act). At June 30, 1991 the Authority was attached to the General Services Administration, whose Administrator is Chairman of the Board of Directors of the Authority and is an integral part of the Commonwealth of Puerto Rico's financial reporting. On July 1, 1991 the Authority, by Act No. 18, was separated from the General Services Administration.

The Authority is empowered to design and construct office buildings, courts, warehouses, shops and related facilities for lease to the Commonwealth or any of its departments, agencies, instrumentalities or municipalities. An amendment to The Enabling Act granted the additional power to finance and construct schools, health-care and social welfare facilities.

The Authority acts in a fiduciary capacity relating to advances received from agencies of the Commonwealth for construction purposes on their behalf. Funds received for these purposes are accounted for separately in the Agency Fund.

The annual rent for each building leased is computed based on the amounts needed by the Authority for: (1) principal, interest and other amortization requirements of the notes and bonds issued to finance the buildings; (2) operating and maintenance expenses of the buildings, including a reasonable proportional share of the Authority's administrative expenses, excluding depreciation; (3) cost of equipment replacement and other noncurrent operating and maintenance costs; and (4) reserve for such purposes. Rentals for operating and maintenance expenses, together with equipment replacement, are subject to escalation to permit the Authority to recover costs in these areas.

The Enabling Act provides that the good faith and credit of the Commonwealth are pledged for the payment of the rentals under any lease agreement executed pursuant to said Enabling Act with any department of the Commonwealth. The Enabling Act also provides that the Commonwealth of Puerto Rico's Department of the Treasury (Treasury Department) will make advances to the Authority for any unpaid portion of rentals payable to the Authority by any agency or instrumentality of the Commonwealth under the lease agreements (See Note 2).

The Authority is exempt from the payment of taxes on its revenues and properties.

#### Accounting Policies

The accounting policies followed by the Authority are based on generally accepted accounting principles adopted for governmental units. A summary of the most significant policies follows:

#### Basis of Presentation

The Authority's financial statements are presented on the basis of two funds namely the Authority's Funds and Agency Fund, each constituting a separate accounting entity which conform to the provisions explained in the preceding paragraphs.

#### Property and Equipment

Property and equipment are stated at cost, except for certain property ($41,000,000) donated by Commonwealth agencies and municipalities which are stated at appraisal value or at the value recorded in the books of the donor at the time of transfer. The cost of the projects constructed by the Authority include a portion of general and administrative expenses and interest allocated during the construction period. Property and equipment with a cost of $1,085,000,000 and $1,030,000,000 for 1992 and 1991, respectively, are leased to governmental agencies. Refer to Note 14.

### Amortization of Discount On Bonds Payable

Discount on bonds payable is amortized over the term of the bonds based on the interest method. Bond issuance costs are generally expensed when incurred.

### Revenue Recognition

All leases are deemed to be operating leases. Accordingly, rent revenue is recognized using the operating method under which income is recognized over the term of the lease.

### Cash Equivalents

Cash equivalents are defined as highly liquid investments with original maturities of 90 days or less.

### Reclassifications

Certain items in the June 30, 1991 financial statements have been reclassified to conform to the classification at June 30, 1992.

## NOTE 2 — RENT RECEIVABLES

In accordance with the provisions of the Enabling Act, the Treasury Department made advances on behalf of certain agency and instrumentality lessees and payments on behalf of certain department lessees. Advances will be reimbursed to the Treasury Department by the Authority when receipt of payment from the agency, instrumentality or department is made. Total advances pending reimbursement and payment on behalf of departmental lessees at June 30, 1992 and 1991, amounted to $11,000.

## NOTE 3 — PROPERTY AND EQUIPMENT

Property and equipment consist of:

| | June 30, 1992 | June 30, 1991 |
|---|---|---|
| Land | $ 52,126,105 | $ 49,056,612 |
| Buildings | 1,030,596,772 | 976,899,314 |
| Furniture and equipment | 2,363,204 | 3,787,634 |
| Construction in progress | 160,708,964 | 139,349,960 |
| | $1,245,795,045 | $1,169,093,520 |

## NOTE 4 — RESTRICTED ASSETS — BOND SINKING FUNDS

The Bond Sinking Funds under Bond Resolutions No. 77 and No. 158 consist of cash and investments valued at cost, which approximate market, as follows:

**June 30, 1992**

| | Bond Service Account | Reserve and Redemption Account | Total |
|---|---|---|---|
| **Resolution No. 77** | | | |
| **Office Buildings** | | | |
| Cash | $ 5,055,543 | $ 461,030 | $ 5,516,573 |
| U.S. Treasury Notes | 8,648,324 | 296,522 | 8,944,846 |
| | 13,703,867 | 757,552 | 14,461,419 |
| **Resolution No. 158** | | | |
| **Public Education and Health Facilities** | | | |
| Cash | $ 42,332,897 | $ 19,534 | $ 42,352,431 |
| | 42,332,897 | 19,534 | 42,352,431 |
| Total restricted assets — bond sinking funds at June 30, 1992 | $ 56,036,764 | $ 777,086 | $ 56,813,850 |

**June 30, 1991**

| | Bond Service Account | Reserve and Redemption Account | Total |
|---|---|---|---|
| **Resolution No. 77** | | | |
| **Office Buildings** | | | |
| Cash | $ 3,377,668 | $ 455,242 | $ 3,832,910 |
| U.S. Treasury Notes | 10,929,205 | — | 10,929,205 |
| | 14,306,873 | 455,242 | 14,762,115 |
| **Resolution No. 158** | | | |
| **Public Education and Health Facilities** | | | |
| Cash | $ 473,454 | $ 193,443 | $ 666,897 |
| U.S. Treasury Notes | 56,432,170 | 2,395,500 | 58,827,670 |
| | 56,905,624 | 2,588,943 | 59,494,567 |
| Total restricted assets — bond sinking funds at June 30, 1991 | $ 71,212,497 | $ 3,044,185 | $ 74,256,682 |

Each Sinking Fund consists of three separate accounts designated "Bond Service Account", "Reserve Account" and "Redemption Account". Debt service rentals received with respect to the facilities financed under Bond Resolutions No. 77 and No. 158 are deposited with their respective Fiscal Agent for the credit of such accounts in the following order:

(a) to the Bond Service Account, such amount as may be required to make the amount equal to the amount of interest then due and payable and the interest which will become due and payable within the next ensuing six months on all bonds of each series then outstanding and the principal of all serial bonds, if any, which will become payable within the next ensuing twelve months;

(b) to the Redemption Account, such amount as may be required to make the amounts so deposited in the then current fiscal year equal to the amortization requirement, if any, for such fiscal year for the term bonds of each series then outstanding, plus the premium, if any, which would be payable on a like principal amount of bonds if such principal amount of bonds should be redeemed on the next redemption date from monies in their respective Bond Sinking Funds; and

(c) the balance, if any, deposited to the credit of the Reserve Account.

Bond Resolution No. 77 requires that monies held in the various accounts be, as nearly as practicable, invested and reinvested in direct obligations of, or obligations the principal of and the interest on which are unconditionally guaranteed by, the United States government. In lieu of such investments, monies in any or all of such accounts may be placed in interest-bearing time deposits. Bond Resolution No. 158 requires that monies be invested and reinvested in investment obligations, repurchase agreements or time deposits fully secured by investment obligations, as those terms are defined therein. Investments will mature or will be subject to redemption by the holder thereof at the option of such holder:

(a) as to investment of monies in the Bond Service Account and the Redemption Account not later than the dates when the monies held for credit thereof will be required for the purposes intended,

(b) as to investment of monies in the Reserve Account under Bond Resolution No. 77 (i) 25% on principal amount not later than the next interest payment date of bonds issued thereunder, (ii) 25% not later than the second interest payment date after such investment, and (iii) 50% not later than three years after the date of such investment, and

(c) as to investment of monies in the Reserve Account under Bond Resolution No. 158 (i) 50% of such monies not later than five years from the date of investment and (ii) the balance of such monies as directed by an order signed by the Executive Director of the Authority.

## NOTE 5 — CONSTRUCTION FUNDS — RESTRICTED

The Authority has various Construction Funds. These Construction Funds are created for the purpose of providing resources for paying all or any part of the remaining cost to the Authority of the Initial Facilities, or for paying all or any part of the cost to the Authority of any Additional Facilities or Improvements, in accordance with the Bond resolutions.

Included in cash are \$12,346,000 and \$14,669,000 at June 30, 1992 and 1991 in certificates of deposits and cash that relate to Construction Funds, which are restricted.

## NOTE 6 — LONG-TERM DEBT

Long-term debt consists of:

| | June 30, | |
|---|---|---|
| | 1992 | 1991 |
| **Office Buildings Bonds:** | | |
| Serial Revenue Bonds, maturing through 2021, interest rates range from 3.80% to $8^3/_5$% | \$ 123,785,000 | \$ 74,585,000 |
| Term Revenue Bonds, maturing through 2021, interest rates range from $5^1/_2$% to $8^7/_8$% | 121,855,000 | 118,500,000 |
| Capital appreciation bonds, maturing through 2006, interest rates range from $6^3/_5$% to $7^3/_{20}$% | 25,877,693 | 24,180,576 |
| | 271,517,693 | 217,265,576 |

| | June 30, 1992 | June 30, 1991 |
|---|---|---|
| **Public Education and Health Facilities Bonds:** | | |
| Serial Bonds, maturing through 2021, interest rates range from 3.80% to 8 3/5% | $ 361,610,001 | $ 211,100,000 |
| Term Bonds, maturing through 2021, interest rates range from 5% to 8 7/8% | 502,145,000 | 519,500,000 |
| Capital Appreciation Bonds, maturing through 2006, interest rates range from 6 3/5% to 7 3/20% | 44,013,854 | 41,176,756 |
| | 907,768,855 | 771,776,756 |
| Total bonds outstanding | 1,179,286,548 | 989,042,332 |
| Less bond discounts | 26,081,375 | 23,712,667 |
| Net bonds payable | 1,153,205,173 | 965,329,665 |
| Notes payable to Government Development Bank for Puerto Rico | — | 34,148,175 |
| Other debt | 2,084,563 | 2,351,068 |
| Total debt | 1,155,289,736 | 1,001,828,908 |
| Less current portion of long-term debt | 22,240,000 | 24,956,660 |
| Total long-term debt | $1,133,049,736 | $ 976,872,248 |

Aggregate maturities of sinkings funds' amortization requirements on bonds and related interest expense in future years are as follows:

| Year ending June 30, | Principal | Interest |
|---|---|---|
| 1993 | $ 22,240,000 | $ 59,757,233 |
| 1994 | 29,235,000 | 74,238,814 |
| 1995 | 40,575,000 | 72,474,549 |
| 1996 | 42,990,000 | 70,060,384 |
| 1997 | 41,910,000 | 67,397,784 |
| Thereafter | 1,002,336,548 | 793,088,698 |
| | $1,179,286,548 | $1,137,017,462 |

The maturities are funded by debt service rentals to be collected from the lessees. The payment of principal and interest on the bonds are guaranteed by the Commonwealth of Puerto Rico to a maximum aggregate principal amount not to exceed $1,200,000,000.

The Authority has redeemed the following bonds during the years ended June 30:

| | 1992 | 1991 |
|---|---|---|
| Office buildings bonds | $ 51,071,660 | $ 7,007,485 |
| Public education and health facilities bonds | 146,935,000 | 15,105,000 |
| Total | $198,006,660 | $22,112,485 |

On August 2, 1992, the Authority issued $43,640,000 Series J Refunding Revenue Bonds, $60,000,000 Series K Revenue Bonds, $130,090,000 Series K Refunding Bonds, and $150,000,000 Series L Public Education and Health Facilities Bonds (Refer to Note 11).

Interest and other financing expenses for the year ended June 30, 1992 and 1991 consist of:

| | 1992 | 1991 |
|---|---|---|
| Total interest and other financing expenses | $79,406,618 | $75,255,566 |
| Less: Interest applied to construction in progress | 9,576,660 | 8,340,904 |
| Net interest and other financing expenses | $69,829,958 | $66,914,662 |

## NOTE 7 — ACCUMULATED NET REVENUES

Accumulated net revenues at June 30, 1992 and 1991 are composed mainly of (1) rentals with respect to principal recorded as income without a corresponding expense (buildings are not depreciated) (Refer to Note 14); (2) interest income and (3) excess of equipment replacement rentals over actual expenses which is appropriated as a reserve for equipment replacement.

## NOTE 8 — RETIREMENT FUND

Substantially all employees of the Authority participate in the Retirement System of the Commonwealth of Puerto Rico (the "System"), a multiple-employer public employee retirement system. The payroll for employees covered by the System for the years ended June 30, 1992 and June 30, 1991 were approximately $23,117,658 and $19,705,429, respectively.

All employees of the Authority who at the time of employment are 55 years old or less are eligible to participate in the System. Employees who retire after 10 years of service are entitled to a retirement benefit, payable monthly for life, which is calculated based on a percentage of the average of the three years of highest salary during the employee's service period. This percentage ranges from 15% at age 58 or older and 10 years of service to 85% at age 55 or older and 35 years of service. The System also provides for death and disability benefits established by Commonwealth statute.

Covered employees are required by Commonwealth statute to contribute 5.775% of their first $550 of monthly salary plus 8.275% for the excess over $550 of monthly salary in one of the alternatives and 8.275% of all salary in the other alternative to the plan. The Authority is required by the same statute to contribute 9.275% of the participant's monthly salary. New participants in the System will contribute 8.275% of the participant's salary. The total contribution requirement for the years ended June 30, 1992 and 1991 was approximately $2,052,213 and $1,924,000, respectively.

The "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement system and employers. The System does not make separate measurements of assets and pension benefit obligations for individual employers. The actuarial present value of accrued benefits obligation at June 30, 1987 (latest date available) for the System as a whole, determined through an actuarial valuation performed as of that date, was $3.2 billion. The System's net assets available for benefits on that date amounted to $619 million, resulting in an excess of accrued benefits over net assets available of $2.6 billion.

Historical trend information regarding the accumulation of assets in the System to pay benefits when due is not available.

## NOTE 9 — COMMITMENTS

The Authority has entered into various contracts with outside contractors for the construction of buildings and other facilities. The Authority records the liability for these contracts as progress billings, based on completed work, as received. The uncompleted portion of these contracts approximated $105,000,000 and $112,000,000 as of June 30, 1992 and 1991, respectively.

## NOTE 10 — CONTINGENT LIABILITIES

The Authority is defendant and/or co-defendant in various lawsuits approximating $3,383,000 for alleged breach of contracts and other actions arising in the ordinary course of business. In the opinion of management, based on advice of legal counsel, the outcome of these lawsuits will not materially affect the financial position of the Authority.

## NOTE 11 — EXTRAORDINARY GAIN (LOSS) — EARLY EXTINGUISHMENT OF DEBT

On April 2, 1992 the Authority defeased $173,050,000 Series A and D Revenue Bonds and Series A and B Public Education and Health Facilities Bonds with net proceeds on the sale of $383,730,000 Series J Revenue Refunding Bonds, Series K Revenue Bonds, Series K Public Education and Health Facilities Refunding Bonds and Series L Public Education and Health Facilities Bonds. The refunding bonds net proceeds were irrevocably deposited; a portion in Escrow Funds with the Fiscal Agents for investment in non-callable direct obligations of the U.S.; the principal of and interest on which when due, with other non-invested moneys, will be sufficient to pay when due the principal of and premium and interest on the Refunded Bonds.

The balance of the funds were used to settle notes payable to the Government Development Bank for Puerto Rico of $38,402,456, deposit $166,122,544 into the 1970 and 1978 Construction Funds and to cover the underwriting and original issue discount and legal, printing and financing expenses of $9,104,132.

The defeasance resulted in an extraordinary accounting loss of $5,230,004. However, as a result of the defeasance the Authority will realize an economic gain over the life of the new bonds issued of approximately $9.7 million.

In prior years, the Authority has defeased certain Revenue Refunding and Public Education and Health Facilities Refunding Bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Authority's financial statements. As of June 30, 1992 $595 million of bonds outstanding are considered defeased.

## NOTE 12 — RESERVE ACCOUNT SUBSTITUTION

During May, 1990 the Authority amended resolutions No. 77 and No. 158 directing the Fiscal Agent to substitute the reserve account with a Reserve Account Letter of Credit and Reserve Account Insurance Policies in order to transfer $94,350,752 in cash and securities from the reserve account to the bond service account. The Authority has the responsibility to credit the debt service rentals for the aforementioned amount to the entities included in Resolution No. 158 as amended, for the period from June 1, 1990 through January 1, 1992.

## NOTE 13 — OFF-BALANCE SHEET RISK AND CONCENTRATION OF CREDIT RISK

The Authority has adopted the Statement of Financial Accounting Standard No. 105, in June 1992, which requires disclosure of information about financial instruments with off-balance sheet risk and about concentrations of credit risk for all financial instruments.

Financial instruments which potentially subject the Authority to concentrations of credit consist principally of temporary cash investments. The Authority places its temporary cash investments with high credit quality financial institutions and limits the amount of credit exposure to any one financial institution.

As of June 30, 1992, the Authority had no significant concentrations of credit risk.

## NOTE 14 — DEPRECIATION

The Authority has excluded from its financial statements depreciation of property and equipment that should be expensed in order to conform with generally accepted accounting principles. If property and equipment were depreciated, property and equipment and capital would have been decreased by $326,404,157 and $291,889,797, respectively, as of June 30, 1992 and 1991, and revenues would have been decreased by $33,992,440 and $31,007,319 for the years ended June 30, 1992 and 1991, respectively.

Management is currently considering various alternatives to deal with this departure from generally accepted accounting principles.

## NOTE 15 — PUBLIC HOUSING PROGRAMS

On May 12, 1992, the Department of Housing of the Commonwealth of Puerto Rico, acting by and through the Administrator of the Public Housing Administration (the "Administration"), entered into an agreement with the Authority, to act as the Administration's agent, for the management of the physical improvement activities under the Department of Housing and Urban Development's (HUD) public housing programs in the Commonwealth of Puerto Rico.

The Administration is the local agency in charge of managing the HUD public housing programs, and to supply the technical resources needed to develop the physical improvements activities of those programs. The Authority has agreed to undertake the management of the following physical improvement activities, in accordance with federal program requirements:

a. Modernization program projects, regardless of their stage;

b. New public housing projects; and

c. Other physical improvement activities.

As of June 30, 1992, the Authority has not received or made any disbursements of federal funds under the HUD public housing programs as per the Agreement.

## NOTE 16 — SAVINGS IN DEBT SERVICE

The Authority eliminated credits in its accounts, related to savings in debt service from a defeasance of bonds. This transaction resulted in rent receivables and capital increasing by $29,243,577 respectively.

## STATEMENT OF CHANGES IN SINKING FUND ACCOUNTS

### AUTHORITY'S FUNDS

**Year ended June 30, 1992**

| OFFICE BUILDING BONDS: | Total | Bond Service Account | Reserve and Redemption Account |
|---|---|---|---|
| Balance at July 1, 1991 | $ 14,762,115 | $ 14,306,873 | $ 455,242 |
| Receipts: | | | |
| Debt service rentals | 21,813,209 | 21,813,209 | — |
| Investment income | 368,377 | 357,628 | 10,749 |
| Bond Proceeds | 556,941 | 556,941 | — |
| Total receipts | 22,738,527 | 22,727,778 | 10,749 |
| Disbursements: | | | |
| Payment of bond interest | 12,987,104 | 12,987,104 | — |
| Payment of bond principal | 7,405,000 | 7,405,000 | — |
| Transfer for Series A, D Refunding | 2,647,119 | 2,647,119 | — |
| Total disbursements | 23,039,223 | 23,039,223 | — |
| Interfund transfer-in (out) | — | (291,561) | 291,561 |
| Balance at June 30, 1992 | $ 14,461,419 | $ 13,703,867 | $ 757,552 |

| PUBLIC EDUCATION AND HEALTH FACILITIES BONDS: | Total | Bond Service Account | Reserve and Redemption Account |
|---|---|---|---|
| Balance at July 1, 1991 | $ 59,494,567 | $ 56,905,624 | $ 2,588,943 |
| Receipts: | | | |
| Debt service rentals | 49,299,455 | 44,475,978 | 4,823,477 |
| Investment income | 3,451,463 | 3,296,223 | 155,240 |
| Bond Proceeds | 1,502,937 | 1,502,937 | — |
| Total receipts | 54,253,855 | 49,275,138 | 4,978,717 |
| Disbursements: | | | |
| Payment of bond interest | 53,352,996 | 53,352,996 | — |
| Payment of bond principal | 17,565,000 | 17,565,000 | — |
| Transfer for Series A, B Refunding | 7,369,558 | 2,528,308 | 4,841,250 |
| Total disbursement | 78,287,554 | 73,446,304 | 4,841,250 |
| Interfund transfer-in (out) | — | 2,517,579 | (2,517,579) |
| Transfer from Construction Funds | 6,891,563 | 6,891,563 | — |
| Balance at June 30, 1992 | $ 42,352,431 | $ 42,143,600 | $ 208,831 |

## STATEMENT OF OPERATING CASH ACCOUNTS

### AUTHORITY'S FUNDS

**Year ended June 30, 1992**

| | Banco Popular | Chase Manhattan Bank |
|---|---|---|
| Balance at July 1, 1991 | $ 594,570 | $ 2,410,118 |
| Deposits: | | |
| Rentals collected, including note and bond debt service rentals amounting to $28,320,724 and $90,959,201 in Banco Popular and Chase Manhattan Bank, respectively | 52,930,955 | 139,431,872 |
| Disbursements: | | |
| For current expenses, transfers to Bond Service Accounts and others | (39,928,055) | (117,582,087) |
| Balance at June 30, 1992* | $ 13,597,470 | $ 24,259,903 |

* Balance included in cash in the accompanying balance sheets.

## STATEMENT OF RENTAL REVENUES AND RECEIVABLES

### AUTHORITY'S FUNDS

| | Revenues Year ended June 30, 1992 | Receivables As of June 30, 1991 |
|---|---|---|
| **Office Buildings** | | |
| Debt service rentals — bonds | $ 24,543,979 | $ 4,877,455 |
| Operating, administrative and equipment replacement reserve rentals | 22,519,546 | 3,872,048 |
| Debt service rentals — notes | — | 545,232 |
| | 47,063,525 | 9,294,735 |
| **Public Education Facilities** | | |
| Debt service rentals — bonds | 43,934,565 | 5,795,227 |
| Debt service rentals — notes | 4,226,579 | 367,457 |
| Debt service rentals — others | 2,250,789 | — |
| Administrative and equipment replacement reserve rentals | 26,753,686 | 3,790,321 |
| | 77,165,619 | 9,953,005 |
| **Health Facilities** | | |
| Debt service rentals — bonds | 25,754,004 | 7,350,227 |
| Debt service rentals — others | 662,779 | 165,695 |
| Administrative and equipment replacement reserve rentals | 9,013,243 | 2,487,039 |
| Debt service rentals — notes | 5,121,321 | 795,581 |
| | 40,551,347 | 10,798,542 |
| Total | $164,780,491 | $ 30,046,282 |

SCHEDULE 4

## STATEMENT OF REVENUES AND EXPENSES AS COMPARED TO BUDGET

### AUTHORITY'S FUNDS

**Year ended June 30, 1992**

| | Actual | Budget |
|---|---|---|
| Revenues: | | |
| Rent: | | |
| Debt-service rentals | $ 106,178,799 | $ 102,724,916 |
| Operating rentals | 58,601,692 | 71,497,780 |
| | 164,780,491 | 174,222,696 |
| Interest and other income | 11,249,060 | 10,576,712 |
| Total revenues | 176,029,551 | 184,799,408 |
| Expenses: | | |
| Interest and other financing expenses | 69,829,958 | 69,149,472 |
| Salaries and employee benefits | 39,472,373 | 40,169,928 |
| Utilities | 8,517,948 | 8,033,740 |
| Repairs and maintenance | 14,378,787 | 8,151,744 |
| Security services | 5,302,185 | 3,431,448 |
| Rent and insurance | 1,422,714 | 1,550,024 |
| Other expenses | 6,463,282 | 2,730,516 |
| | 145,387,247 | 133,216,872 |
| Less administrative expenses applied to construction work in progress | 4,749,218 | 4,495,236 |
| Total expenses | 140,638,029 | 128,721,636 |
| Revenues in excess of expenses before extraordinary loss | 35,391,522 | 56,077,772 |
| Extraordinary (loss) — extinguishment of debt | (5,230,004) | — |
| Net revenues in excess of expenses | $ 30,161,518 | $ 56,077,722 |

SCHEDULE 5

## STATEMENT OF CAPITAL IMPROVEMENTS PROGRAM AS COMPARED TO BUDGET

### AUTHORITY'S FUNDS

**Year ended June 30, 1992**

| | Actual | Budget |
|---|---|---|
| Education Facilities | $11,564,746 | $ 48,203,118 |
| Health and Welfare Facilities | 34,743,412 | 15,436,655 |
| Office Buildings | 31,817,795 | 39,011,964 |
| Authority's Equipment, net of a write off of approximately $1.9 million | (1,424,427) | 487,587 |
| Total | $76,701,526 | $103,139,324 |

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FACSIMILE: 071-796-1807

June , 1993

PUERTO RICO PUBLIC BUILDINGS AUTHORITY
San Juan, Puerto Rico

Gentlemen:

We have examined Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended (hereinafter called the "Enabling Act"), creating Public Buildings Authority (the "Authority") as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth") exercising public and essential governmental functions. We have also examined Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (hereinafter called the "Guaranty Act"), providing for the guaranty by the Commonwealth of the payment of the principal of and interest on a principal amount of bonds outstanding at any one time of the Authority, not exceeding $1,200,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose.

We have also examined certified copies of the proceedings of the Authority, including Resolution No. 77, adopted on November 16, 1970, as supplemented (said Resolution No. 77, as supplemented, being hereinafter called the "Bond Resolution"), and other proofs submitted relative to the authorization, sale and issuance of the following described bonds (collectively, the "Bonds"):

**$128,895,000**
**PUBLIC BUILDINGS AUTHORITY**
**REVENUE REFUNDING BONDS, SERIES L**
**GUARANTEED BY THE COMMONWEALTH OF PUERTO RICO**

issued in such denominations, transferable and exchangeable, dated, bearing interest at such rates (or having such yields) and payable on such dates, maturing on July 1 of the years and in such principal amounts, and subject to redemption prior to maturity, all as set forth in the resolution of the Authority authorizing the issuance of the Bonds.

We have also examined one of the Bonds as executed and authenticated.

From such examination we are of the opinion that:

1. The Enabling Act is valid.

2. The Guaranty Act is valid.

3. Said proceedings have been validly and legally taken.

4. The Bonds have been duly authorized and issued to provide funds to refund in advance of maturity the Authority's outstanding Public Buildings Authority Revenue Bonds, all guaranteed by the Commonwealth: Series B due July 1, 2002; Series H due July 1 in the years 1999, 2009, 2017 and 2019; and Series K due July 1 in the years 2003 through 2005, 2007, 2012 and 2021; and the Bonds are valid and binding obligations of the Authority payable solely from the special fund created by the Bond Resolution and designated "Puerto Rico Public Buildings Authority Revenue Bonds Interest and Sinking Fund" (the "Sinking Fund") or from moneys provided by the Commonwealth under its guaranty of payment of the principal of and interest on the Bonds. The Authority has covenanted to deposit to the credit of the Sinking Fund a sufficient amount of the rentals received by the Authority from the leasing of office buildings financed by the Authority under the provisions of the Bond Resolution to pay the principal of and the redemption premium, if any, and the interest on all bonds issued under the provisions of the Bond Resolution as the same become due, which Sinking Fund is pledged to and charged with the payment of such principal, redemption premium, if any, and interest.

5. The Authority has properly specified the Bonds to be covered by the guaranty of the Commonwealth under the Guaranty Act.

6. The good faith and credit of the Commonwealth are pledged for the payment of any amounts required to be paid by the Commonwealth pursuant to said guaranty.

7. The Bond Resolution provides for the issuance, from time to time, under the conditions, limitations and restrictions therein set forth, of additional bonds for the purpose of paying all or a part of the cost of additional office buildings and improvements of office buildings and refunding any bonds issued by the Authority under the provisions of the Bond Resolution.

8. Under the provisions of the Acts of Congress now in force and under existing regulations and judicial decisions, (i) subject to compliance with the covenant referred to below and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), regarding the use, expenditure and investment of bond proceeds and the timely payment of certain investment earnings to the Treasury of the United States, if required, interest on the Bonds is not includable in gross income for federal income tax purposes and (ii) the Bonds and the interest thereon are exempt from state, Commonwealth and local income taxation.

Interest on the Bonds is not an item of tax preference for the purpose of computing the alternative minimum tax on individuals imposed by the Code. Such interest will, however, be includable in the computation of the alternative minimum tax and the environmental tax on corporations imposed by the Code. The Code contains other provisions that could result in tax consequences, upon which we express no opinion, as a result of (a) ownership of the Bonds or (b) the inclusion in certain computations (including, without limitation, those related to the corporate alternative minimum tax and environmental tax) of interest that is excluded from gross income.

The Authority has covenanted to comply with the requirements of the Code, to the extent permitted by the Constitution and laws of the Commonwealth, so that interest on the Bonds will remain exempt from federal income taxes to which it is not subject on the date of issuance of the Bonds.

Respectively submitted

[To be signed "Brown & Wood"]

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June , 1993

PUERTO RICO PUBLIC BUILDINGS AUTHORITY
San Juan, Puerto Rico

Gentlemen:

We have examined Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended (hereinafter called the "Enabling Act"), creating Public Buildings Authority (the "Authority") as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth") exercising public and essential governmental functions. We have also examined Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (hereinafter called the "Guaranty Act"), providing for the guaranty by the Commonwealth of the payment of the principal of and interest on a principal amount of bonds outstanding at any one time of the Authority, not exceeding $1,200,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose.

We have also examined certified copies of the proceedings of the Authority, including Resolution No. 158, adopted on February 14, 1978, as supplemented (said Resolution No. 158, as supplemented, being hereinafter called the "Bond Resolution"), and other proofs submitted relative to the authorization, sale and issuance of the following described bonds (collectively, the "Bonds"):

**$584,585,000**
**PUBLIC BUILDINGS AUTHORITY**
**PUBLIC EDUCATION AND HEALTH FACILITIES REFUNDING BONDS, SERIES M**
**GUARANTEED BY THE COMMONWEALTH OF PUERTO RICO**

issued in such denominations, transferable and exchangeable, dated, bearing interest at such rates (or having such yields) and payable on such dates, maturing on July 1 in the years and in such principal amounts, and subject to redemption prior to maturity, all as set forth in the resolution of the Authority authorizing the issuance of the Bonds.

We have also examined one of the Bonds as executed and authenticated.

From such examination we are of the opinion that:

1. The Enabling Act is valid.

2. The Guaranty Act is valid.

3. Said proceedings have been validly and legally taken.

4. The Bonds have been duly authorized and issued to provide funds to refund the following series of the Authority's outstanding Public Buildings Authority Public Education and Health Facilities Bonds, all guaranteed by the Commonwealth: Series F, due July 1 in the years 1997 through 2004 and 2012; Series G, due July 1 in the years 1998 through 2002, 2007 and 2016; Series H, due July 1 in the years 1998 through 2002, 2007 and 2016; Series J, due July 1 in the years 1999, 2009, 2017 and 2019; and Series L due July 1 in the year 2003 through 2005, 2007, 2012 and 2021; and the Bonds are valid and binding obligations of the Authority payable solely from the special fund created by the Bond Resolution and designated "Puerto Rico Public Buildings Authority Public Education and Health Facilities Bonds Interest and Sinking Fund" (the "Sinking Fund") or from moneys provided by the Commonwealth under its guaranty of payment of the principal of and interest on the Bonds. The Authority has covenanted to deposit to the credit of the Sinking Fund a sufficient amount of the rentals received by the Authority from the leasing of school and related facilities and health and related facilities financed or refinanced by the Authority under the provisions of the Bond Resolution to pay the principal of and the redemption premium, if any, and the interest on all bonds issued under the provisions of the Bond Resolution as the same become due, which Sinking Fund is pledged to and charged with the payment of such principal, redemption premium, if any, and interest.

5. The Authority has properly specified the Bonds to be covered by the guaranty of the Commonwealth under the Guaranty Act.

6. The good faith and credit of the Commonwealth are pledged for the payment of any amounts required to be paid by the Commonwealth pursuant to said guaranty.

7. The Bond Resolution provides for the issuance, from time to time, under the conditions, limitations and restrictions therein set forth, of additional bonds for the purpose of paying all or a part of the cost of school and related facilities and health and related facilities and improvements of such facilities and refunding any bonds issued by the Authority under the provisions of the Bond Resolution.

8. Under the provisions of the Acts of Congress now in force and under existing regulations and judicial decisions, (i) subject to compliance with the covenant referred to below and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), regarding the use, expenditure and investment of bond proceeds and the timely payment of certain investment earnings to the Treasury of the United States, if required, interest on the Bonds is not includable in gross income for federal income tax purposes and (ii) the Bonds and the interest thereon are exempt from state, Commonwealth and local income taxation.

Interest on the Bonds is not an item of tax preference for the purpose of computing the alternative minimum tax on individuals imposed by the Code. Such interest will, however, be includable in the computation of the alternative minimum tax and the environmental tax on corporations imposed by the Code. The Code contains other provisions that could result in tax consequences, upon which we express no opinion, as a result of (a) ownership of the Bonds or (b) the inclusion in certain computations (including, without limitation, those related to the corporate alternative minimum tax and environmental tax) of interest that is excluded from gross income.

The Authority has covenanted to comply with the requirements of the Code, to the extent permitted by the Constitution and laws of the Commonwealth, so that interest on the Bonds will remain exempt from federal income taxes to which it is not subject on the date of issuance of the Bonds.

Respectfully submitted,

[To be signed "Brown & Wood"]

## DESCRIPTION OF THE TAX EXEMPT COMPONENTS

The terms of the Tax Exempt Components ("TXCs") are as described below.

### General

The $5,120,000 aggregate principal amount of 1993 Revenue Refunding Bonds maturing January 1, 2007 and $5,400,000 aggregate principal amount of 1993 Revenue Refunding Bonds maturing July 1, 2008 (the "TXC 1993 Revenue Refunding Bonds") and $30,000,000 aggregate principal amount of 1993 Public Education and Health Facilities Refunding Bonds maturing July 1, 2007 and $31,640,000 aggregate principal amount of 1993 Public Education and Health Facilities Refunding Bonds maturing July 1, 2008 (the "TXC 1993 Public Education and Health Facilities Refunding Bonds"; and with the TXC 1993 Revenue Refunding Bonds, the "1993 TXC Bonds") will be delivered as Current Interest TXCs. As described more fully below, TXCs will consist of Single Coupon TXCs; Principal Only TXCs; Annuity TXCs; Deferred Interest TXCs; and Current Interest TXCs.

TXCs will be issued in fully registered form, will be dated June 1, 1993 and will evidence the obligation of the Authority to make one or more interest and/or principal payments to the registered owner of such TXC at the times and in the amounts specified in such TXC (each such payment date being on January 1 or July 1 and being referred to hereinafter as a "TXC Payment Date"). The final payment under any TXC will be made on the date specified in such TXC (each, a "TXC Termination Date"), which in no event will be later than the applicable maturity date of the related 1993 TXC Bond (each, a "1993 TXC Bond Final Maturity Date"). The TXCs are issuable in denominations of $5,000 principal amount or Notional Principal Amount (as defined below) and any multiple thereof.

Those TXCs which obligate the Authority to make more than one payment to the registered owner are referred to herein as Periodic TXCs ("PTXCs"), and those TXCs which obligate the Authority to make only one payment to the registered owner are referred to herein as Single TXCs ("STXCs"). Each PTXC will evidence ownership of a combination of linked STXCs and any PTXC may be seperated into other TXCs as described under the caption "Linkage of TXCs" below.

### Definitions

There follows a description of each TXC being offered. For purposes of such description, the following terms are used:

"Notional Principal Amount" means that dollar amount specified in a TXC as the amount to be multiplied by the applicable TXC Bond Rate specified in such TXC in order to determine the amount of (a) the payment due on an STXC or (b) the payments due on PTXC.

"TXC Bond Rate" means 5.50% per annum in respect of TXCs relating to 1993 TXC Bonds maturing July 1, 2007 and 5.60% per annum in respect of TXCs relating to 1993 TXC Bonds maturing July 1, 2008.

"TXC Regular Record Date" means the second Business Day immediately preceding a TXC Payment Date.

### Types of TXCs

The TXCs may evidence the following obligations of the Authority expressed in minimum denominations of $5,000 principal amount or Notional Principal Amount.

1. *A Single Coupon TXC* is a STXC which obligates the Authority to pay the registered owner one of the semiannual interest payments due on the related 1993 TXC Bond on each January 1 and July 1, commencing January 1, 1994, to and including the applicable 1993 TXC Bond Final Maturity Date. There will not be any payments on Single Coupon TXCs, nor will Single Coupon TXCs be redeemable prior to the applicable TXC

Termination Date. On the TXC Termination Date, the registered owner of a Single Coupon TXC is due a single payment of the face amount of such Single Coupon TXC.

2. *A Principal Only TXC* is a STXC which obligates the Authority to pay the registered owner an amount equal to $5,000 on the applicable TXC Termination Date. There will not be any payments on Principal Only TXCs, nor will Principal Only TXCs be redeemable prior to the applicable TXC Termination Date.

3. *An Annuity TXC* is a PTXC which obligates the Authority to pay the registered owner all of the semiannual interest payments due on the related 1993 TXC Bond on each January 1 and July 1, commencing January 1, 1994, to and including the applicable 1993 TXC Bond Final Maturity Date. Annuity TXCs are not redeemable prior to their respective TXC Payments Dates.

4. *A Deferred Interest TXC* is a PTXC which obligates the Authority to pay the registered owner $5,000 on the applicable TXC Termination Date plus all of the semiannual interest payments due on the related 1993 TXC Bond on each January 1 and July 1, commencing January 1, 2004, to and including the applicable 1993 TXC Bond Final Maturity Date. Deferred Interest TXCs are not redeemable prior to their respective TXC Payment Dates.

5. *A Current Interest TXC* is a PTXC which obligates the Authority to pay $5,000 to the registered owner on the applicable TXC Termination Date plus all of the semiannual interest payments due on the related 1993 TXC Bond on each January 1 and July 1, commencing January 1, 1994 to and including the applicable 1993 TXC Bond Final Maturity Date. Current Interest TXCs are not redeemable prior to their respective TXC Payment Dates. Ownership of a Current Interest TXC is equivalent to ownership of a 1993 TXC Bond.

The following table sets forth the TXC CUSIP Numbers:

| | Related TXC Bonds | | | |
|---|---|---|---|---|
| **Description of TXC** | **Series L Due July 1, 2007** | **Series L Due July 1, 2008** | **Series M Due July 1, 2007** | **Series M Due July 1, 2008** |
| Single Coupon TXC | 745235 (1) | 745235 (1) | 745232 (1) | 745232 (1) |
| Principal Only TXC | 745235 JY8 | 745235 KE0 | 745232 NH7 | 745232 NP9 |
| Annuity TXC | 745235 JV4 | 745235 KC4 | 745232 NE4 | 745232 NM6 |
| Deferred Interest TXC | 745235 JU6 | 745235 KB6 | 745232 ND6 | 745232 NL8 |
| Current Interest TXC | 745235 JZ5 | 745235 GG0 | 745232 NJ3 | 745232 KR8 |

(1) CUSIP Numbers for each Single Coupon TXC commencing with the STXC evidencing the interest payment due January 1, 1994 and ending with the STXC evidencing the interest payment due on the applicable 1993 TXC Bond Final Maturity Date have been assigned and will be available from the Linkage Agent.

A minimum denomination for each Single Coupon TXC and Annuity TXC will be recorded on the books and records of the Securities Depository as if the particular TXC entitled the Beneficial Owner to payment of the $5,000 Notional Principal Amount. Thus, for example, a Beneficial Owner of a minimum denomination Annuity TXC will be credited on the books and records of the Securities Depository with $5,000 under the appropriate CUSIP number. Beneficial Owners of TXCs should note that this crediting indicates that such Owner is entitled to the payment due on such TXC in a minimum denomination, not that such TXC represents an obligation to pay $5,000.

### Linkage of TXCs

**Linking.** An owner of one or more TXCs may link such TXCs with one or more other TXCs (but only TXCs relating to 1993 TXC Bonds with the same Final Maturity Date and only if such TXCs are represented by a global bond registered in the name of the Securities Depository or its nominee), by purchasing such TXCs and, in each case, delivering to the Linkage Agent a request for linkage (a "Linkage Request") pertaining to the TXC to be linked and taking such other action as the Linkage Agent requests. The Linkage Agent shall note on its books and records the linked TXCs, including reference to the applicable CUSIP numbers. After linkage, the beneficial ownership of linked TXCs will be recorded at the Securities Depository (if the TXCs are then held in book-entry only form) under the applicable CUSIP number.

**TXCs may not be linked, nor may linkage be broken during the period commencing on the TXC Record Date and ending prior to the opening of business on such TXC Payment Date (the "TXC Closed Period"), and the transfer of TXCs that are linked may only be registered together as linked securities.**

**Breaking Linkage of TXCs.** An owner of linked TXCs may break such linkage at any time, other than during a TXC Closed Period, into a combination of STXCs, Annuity TXCs, Principal Only TXCs and/or Deferred Interest TXCs having the same aggregate cash flow characteristics as such linked TXCs by delivering a request to break linkage to the Linkage Agent (a "Request To Break Linkage") and taking such other action as the Linkage Agent shall request. Following the breaking of linkage, the Linkage Agent shall note on its books and records the breaking of linkage, including reference to the applicable CUSIP numbers. The beneficial ownership of unlinked TXCs will be recorded at the Securities Depository (if the TXCs are then held in book-entry only form) under the applicable separate CUSIP numbers.

**Linkage Agent**

The Chase Manhattan Bank, N.A. (the "Linkage Agent") will serve as the initial Linkage Agent. Any successor Linkage Agent must be an entity that would be qualified to serve as fiscal agent under the applicable Bond Resolution and be authorized by law to perform all the duties imposed upon it. The Linkage Agent may be removed by the Fiscal Agents at any time upon and pursuant to the written direction of the owners of 66⅔% in aggregate Accreted Value of the TXCs then Outstanding, and the Linkage Agent may resign upon 30 days' written notice delivered to the Fiscal Agents; provided that such removal or resignation will not take effect until the appointment by the Fiscal Agents of a successor Linkage Agent. The Authority will provide the Fiscal Agents with directions which will enable the Fiscal Agents to appoint a successor Linkage Agent that is a qualified institution; provided, however, that if the Fiscal Agents are unable to appoint a successor Linkage Agent within 30 days following receipt of any written notice of resignation, the Fiscal Agents may (but are under no obligation to do so unless provided adequate compensation and indemnity) petition the appropriate court having jurisdiction to appoint a successor Linkage Agent.

**Special Considerations**

**THE AUTHORITY IS NOT OBLIGATED TO PROVIDE TXCs TO AN OWNER OF TXCs WHO DESIRES TO LINK TXCs. IN ORDER TO LINK TXCs, AN OWNER MUST ACQUIRE THE REQUIRED TXCs IN THE SECONDARY MARKET.**

**THE FIRST BOSTON CORPORATION HAS ADVISED THE AUTHORITY THAT IT INTENDS INITIALLY TO MAKE A MARKET FOR THE TXCs; HOWEVER, THE FIRST BOSTON CORPORATION IS NOT OBLIGATED TO MAKE SUCH MARKET AND MAY DISCONTINUE MAKING SUCH MARKET WITHOUT NOTICE AT ANY TIME. NEITHER THE AUTHORITY NOR THE FIRST BOSTON CORPORATION CAN GIVE ANY ASSURANCE THAT A SECONDARY MARKET WILL DEVELOP FOR THE TXCs. THE ABSENCE OF SUCH SECONDARY MARKET COULD PREVENT THE LINKAGE OF TXCs AND ADVERSELY AFFECT THE LIQUIDITY OF INVESTMENTS IN TXCs.**

**Voting Rights of Owners of TXCs Following Events of Default**

If a vote of the Owners of TXCs is required or called for under the terms of the applicable Bond Resolution, each TXC shall be deemed to evidence a principal amount of TXCs Outstanding that is equal to the accreted value of the TXCs on the date on which the applicable Fiscal Agent determines to fix such accreted value.Such accreted values will be based on a yield of 5.575% per annum with respect to TXCs relating to 1993 TXC Bonds due July 1, 2007 and 5.625% per annum with respect to TXCs relating to 1993 TXC Bonds due July 1, 2008 compounded semiannually to the TXC Termination Date (in respect of STXCs) and TXC Payment Dates (in respect of PTXCs).

In the case of a vote, the applicable Fiscal Agent shall fix the Accreted Value on the Business Day preceding the day on which the applicable Fiscal Agent mails notice of the matter on which the vote is required to holders of TXCs.

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# DESCRIPTION OF THE INDEXED INVERSE FLOATERS

The terms of the Indexed Inverse Floaters are as described below.

*General.* Interest with respect to the Indexed Inverse Floaters will be payable in arrears on January 1 and July 1 of each year, commencing January 1, 1994, to the owners thereof as of the Indexed Inverse Floaters Record Date preceding such Interest Payment Date and shall be computed using a year of 360 days comprised of twelve 30-day months.

Interest with respect to Indexed Inverse Floaters will accrue (i) from the date of initial delivery through the day prior to the Scheduled Conversion Date, at a rate per annum equal to the Indexed Inverse Floaters Rate and (ii) from and after the Scheduled Conversion Date, at a rate per annum equal to the Base Rate. In addition, if there is an optional conversion of Indexed Inverse Floaters as described below, such Indexed Inverse Floaters will bear interest from the Interest Payment Date immediately preceding the Optional Conversion Date (or, (i) if the Optional Conversion Date occurs prior to the Indexed Inverse Floaters Record Date immediately preceding the first Interest Payment Date, the Effective Date or (ii) if the Optional Conversion Date is an Interest Payment Date, such Interest Payment Date) to the day prior to the Scheduled Conversion Date at the applicable Converted Rate.

*Swap Transaction.* The Authority, prior to the initial delivery of the Indexed Inverse Floaters, will enter into an interest rate swap agreement (the "Master Agreement") with Government Development Bank for Puerto Rico ("GDB"). Simultaneously with, and as a condition to, the delivery of the Indexed Inverse Floaters, the Authority will enter into a rate swap transaction (the "Rate Swap Transaction") in accordance with the Master Agreement, pursuant to the terms of which the Authority will be required to pay GDB a variable rate equal to the product of the Leverage Factor times the Index Rate (not to exceed the Maximum Rate) and be entitled to receive from GDB a fixed rate equal to the product of the Leverage Factor times the Fixed Swap Rate on a notional amount equal to the principal amount of Indexed Inverse Floaters. The Rate Swap Transaction commences on the Effective Date and terminates on the Scheduled Conversion Date. The Authority intends to use such payments to offset any interest payments due on the Indexed Inverse Floaters in excess of interest at the rate of 5.70% per annum. However, such arrangements will not affect the obligation of the Authority under the 1978 Bond Resolution to provide funds sufficient to pay the principal of and the interest on the Indexed Inverse Floaters (as such interest may be adjusted upon optional conversion of Indexed Inverse Floaters as described below). No payments are to be made by GDB to the 1978 Fiscal Agent on behalf of the Bondowners under the Rate Swap Transaction, and neither the 1978 Fiscal Agent nor the Bondowners have any pledge or lien on such payments.

*Certain Definitions.* As used with respect to the Indexed Inverse Floaters, the following terms shall have the meanings indicated.

"Base Rate" means 5.70% per annum.

"Business Day" means any day except Saturday, Sunday or any day on which banking institutions located in the State of New York or the Commonwealth of Puerto Rico are required or authorized to close or on which the New York Stock Exchange is closed.

"Conversion Date" means the earlier to occur of the Scheduled Conversion Date or an Optional Conversion Date.

"Converted Rate" means, for any Indexed Inverse Floaters converted on an Optional Conversion Date, the interest rate for the period beginning on the Interest Payment Date next preceding such Optional Conversion Date (or, (i) if the Optional Conversion Date occurs prior to the Indexed Inverse Floaters Record Date immediately preceding the first Interest Payment Date, the Effective Date or (ii) if the Optional Conversion Date is an Interest Payment Date, such Interest Payment Date) and ending on, but not including, the Scheduled Conversion Date, which interest rate shall equal the Base Rate plus the Interest Rate Adjustment for such Indexed Inverse Floaters.

"Effective Date" means June 16, 1993.

"Fixed Swap Rate" means 3.76%.

"Index" means the PSA Municipal Swap Index™, as published in "The Bond Buyer", or if the PSA Municipal Swap Index™ is no longer published, an index selected by the Market Agent in consultation with the Authority.

"Index Rate" means for each Interest Period a rate equal to a per annum rate expressed as a decimal, calculated by multiplying the Relevant Rate in effect for each day of the Interest Period by the number of days such Relevant Rate is in effect, determining the sum of such products and dividing such sum by the number of days in the Interest Period.

"Indexed Inverse Floaters Rate" means a rate equal to the result of 11.34% minus the product of the Leverage Factor times the Index Rate. In no event will the Indexed Inverse Floaters Rate be less than zero for any Interest Period or greater than the Maximum Rate.

"Indexed Inverse Floaters Record Date" means the 15th day of the month next preceding each Interest Payment Date.

"Interest Payment Date" means January 1, 1994 and each January 1 and July 1 thereafter.

"Interest Period" means each period from and including one Interest Payment Date to but excluding the next following Interest Payment Date, except that the initial Interest Period will be the period from and including the date of delivery of the Indexed Inverse Floaters and ending on and excluding January 1, 1994.

"Interest Rate Adjustment" means the Interest Rate Adjustment calculated as described under the caption *"Determination of Converted Rate"* below.

"Leverage Factor" means 1.5 (one and one-half).

"Market Agent" means The First Boston Corporation or such other entity as The First Boston Corporation and the Authority may mutually agree upon.

"Maximum Rate" means 11.34%.

"Relevant Rate" means, for any day, a per annum rate, expressed as decimal, equal to:

(i) if such day is a Reset Date, the Index; and

(ii) if such day is not a Reset Date, the Index for the next preceding Reset Date.

"Reset Date" means each Thursday of an Interest Period or, if any Thursday is not a Business Day, the first succeeding Business Day which is not the last day of an Interest Period or, if any Thursday is a Business Day and is the last day of an Interest Period, the next succeeding Business Day; provided, however, that if the date of issuance of the Indexed Inverse Floaters is a day other than a Thursday, the first Reset Date shall be the Thursday next preceding such date of issuance or, if such Thursday is not a Business Day, the first succeeding Business Day. For the purposes of this provision "Business Day" means any day other than a Saturday, Sunday, a day on which commercial banks in New York City are required to be closed or a day on which the New York Stock Exchange is closed.

"Scheduled Conversion Date" means July 1, 1998.

*Special Considerations.* Prospective purchasers of the Indexed Inverse Floaters should note that because the interest rate with respect to Indexed Inverse Floaters prior to a Conversion Date will be determined by subtracting the product of the Leverage Factor times the Index Rate from a fixed amount, the interest rate with respect to the Indexed Inverse Floaters prior to a Conversion Date will:

*decrease* as the Index Rate *increases,* and

*increase* as the Index Rate *decreases.*

In addition, as a result, the Indexed Inverse Floaters Rate prior to a Conversion Date will equal zero if the Index Rate multiplied by the Leverage Factor is equal to or greater than 11.34% per annum.

*Optional Conversion of Indexed Inverse Floaters.* On any Business Day prior to the Scheduled Conversion Date, the owner of Indexed Inverse Floaters may elect to convert the interest rate payable on not less than $5,000,000 principal amount of such Indexed Inverse Floaters to the Converted Rate.

Such election shall be made by delivery by the owner of such Indexed Inverse Floaters of written or telephonic notice, to the Market Agent (The First Boston Corporation (Attention: Municipal Financial Products, Park Avenue Plaza, 55 East 52nd Street, New York, New York 10055, Facsimile No. (212) 909-1452, Telephone: (212) 902-3202 or such other number as The First Boston Corporation shall designate to the Authority) by 11:00 A.M., New York City time, on the Business Day prior to the proposed Optional Conversion Date (the "Notice Date") specifying (i) the principal amount of such Indexed Inverse Floaters to be converted, (ii) the proposed Optional Conversion Date, (iii) the method by which the Market Agent will be able to contact such owner between 11:00 A.M. and 2:00 P.M., New York City time, on the Notice Date and (iv) evidence satisfactory to the Market Agent that such owner is the owner of the Indexed Inverse Floaters being converted.

Prior to 2:00 P.M., New York City time, on the Notice Date, the Market Agent shall determine (i) whether the Indexed Inverse Floaters will be converted, (ii) the Optional Conversion Date and (iii) the applicable Converted Rate and shall make reasonable efforts to advise the owner using the method specified in the notice, as to such determinations. Any determination made by the Market Agent pursuant to this paragraph shall be binding until 3:00 P.M., New York City time, on the Notice Date, provided there shall have been no material adverse change in the market for interest rate exchange agreements based on tax-exempt market interest rates prior to such time. If, in the exclusive judgment of the Market Agent, such material adverse change shall have occurred, the Market Agent shall rescind such determination by not providing the telephonic confirmation referred to in the following paragraph.

The owner shall provide telephonic notice to the Market Agent of its offer to convert its Indexed Inverse Floaters to the so determined Converted Rate not later than 3:00 P.M., New York City time, on the Notice Date. Such notice shall be irrevocable; provided, that the conversion shall be effective only if the Market Agent shall at such time on such Notice Date, by telephone, confirm its acceptance of the Converted Rate. Immediately following such confirmation, the owner shall, in the event that the Indexed Inverse Floaters are registered in the name of Cede & Co., as nominee for DTC, provide the Participant through which such owner holds such Indexed Inverse Floaters irrevocable written notice to convert the interest on such Indexed Inverse Floaters.

Not later than 5:00 P.M., New York City time, on the Notice Date, the Owner shall provide to the Authority, the 1978 Fiscal Agent and the Market Agent irrevocable written notice (i) specifying the converted Indexed Inverse Floaters, (ii) acknowledging that such Indexed Inverse Floaters bear interest at the Converted Rate, and (iii) providing evidence satisfactory to the Market Agent (X) that such owner is the owner of the converted Indexed Inverse Floaters and (Y) (I) in the event that the Indexed Inverse Floaters are registered in the name of Cede & Co., as nominee for DTC, that there shall have been provided to the Participant through which such owner holds such Indexed Inverse Floaters irrevocable written notice to convert the interest rate on such Indexed Inverse Floaters or authorizing the Market Agent to provide such notice, or (II) in any other event, that the owner shall surrender to the 1978 Fiscal Agent for conversion its Indexed Inverse Floaters. Failure by the owner to deliver the notice described in the preceding sentence shall not affect the conversion made in the telephonic notice provided by the owner in the immediately preceding paragraph.

Notwithstanding anything contained under this heading, the Optional Conversion Date for any Indexed Inverse Floaters for which the owner has provided notice of conversion (as described in the fourth preceding paragraph) during the period beginning on the Indexed Inverse Floaters Record Date and ending on the next succeeding Interest Payment Date shall be a date not earlier than such next succeeding Interest Payment Date.

*Determination of Converted Rate.* Upon receipt of notice from an owner of its election to convert Indexed Inverse Floaters to the Converted Rate as provided above, the Market Agent shall determine the Interest Rate Adjustment. The Interest Rate Adjustment shall be equal to the difference obtained by subtracting from the product of the Leverage Factor times the Fixed Swap Rate, the fixed per annum rate (applied on the basis of a year of 360 days comprised of twelve 30-day months) that would be payable to GDB semiannually on January 1 and July 1 over the period beginning on the first January 1 or July 1 after the Optional Conversion Date (or on the Optional Conversion Date if the Optional Conversion Date is an Interest Payment Date) and ending on the day prior to the Scheduled Conversion Date, in order to unwind a hypothetical swap agreement with the same terms as the Rate Swap Transaction. GDB shall pay such Interest Rate Adjustment if such difference is positive; such Interest Rate Adjustment shall be paid to GDB if such difference is negative. The agreement to unwind the hypothetical swap agreement is assumed to be with a party having generally the same credit rating as the Authority under which GDB agrees to pay the Leverage Factor times the Index Rate (not to exceed the Maximum Rate) and to receive in return a fixed rate over the period beginning on the last January 1 or July 1 preceding the Optional Conversion Date (or, (i) if the Optional Conversion Date occurs prior to the Indexed Inverse Floaters Record Date immediately preceding the first Interest Payment Date, the Effective Date or (ii) if the Optional Conversion Date is an Interest Payment Date, such Interest Payment Date) and ending on the day prior to the Scheduled Conversion Date, including any amounts that would have accrued but been unpaid as of the Optional Conversion Date on a notional amount equal to the principal amount of Indexed Inverse Floaters being converted. Any Interest Rate Adjustment payable by GDB shall be expressed as a positive number and any Interest Rate Adjustment payable to GDB shall be expressed as a negative number.

From and after the Interest Payment Date next preceding an Optional Conversion Date (or, (i) if the Optional Conversion Date occurs prior to the Indexed Inverse Floaters Record Date immediately preceding the first Interest Payment Date, the Effective Date or (ii) if the Optional Conversion Date is an Interest Payment Date, such Interest Payment Date) and prior to the Scheduled Conversion Date, the converted Indexed Inverse Floaters shall bear interest at the Converted Rate. The Converted Rate shall be equal to the Base Rate plus the Interest Rate Adjustment. In no event will the Converted Rate be more than the Maximum Rate per annum or be less than zero.

Prospective owners of Indexed Inverse Floaters should note that it is not possible to determine at this time the amount of any Interest Rate Adjustment. Such amounts are subject to conditions in the tax-exempt interest rate exchange market at the times of conversions. Any such amount is expected, however, to approximate the replacement costs for GDB of the notional amount of the Rate Swap Transaction being reversed in order to effect such conversion. Such replacement cost is expected to be approximately equal to the cost of preserving to GDB the economic equivalent of the payment obligations of the Authority following the Optional Conversion Date. If an Interest Rate Adjustment is positive, the Authority will pay, and an owner will receive, an interest rate in excess of the Base Rate. If the Interest Rate Adjustment is negative, the Authority will pay, and an owner will receive, an interest rate less than the Base Rate.

Generally, upon the Optional Conversion of an Indexed Inverse Floater, (i) the Converted Rate will exceed the applicable Base Rate if fixed payor rates in the market for interest rate exchange transactions based on tax-exempt market interest rates are less than the Fixed Swap Rate and (ii) the Converted Rate will be less than the applicable Base Rate if fixed payor rates in the market for interest rate exchange transactions based on tax-exempt market interest rates exceed the Fixed Swap Rate.

*Conditions to Optional Conversion.* Any Optional Conversion is expressly conditioned on the following:

(a) the Market Agent is providing swap quotations on the basis of tax-exempt market interest rates;

(b) the Indexed Inverse Floaters have a rating in one of the three highest rating categories of Moody's Investors Service or Standard & Poor's Corporation (or their successors), provided that the Market Agent shall have the right to waive the condition set forth in this clause (b) if the 1978 Fiscal Agent shall have received an opinion of nationally recognized bond counsel to the effect that such waiver would not adversely affect the tax-exempt status of the interest on the Indexed Inverse Floaters;

(c) the Optional Conversion does not expose the Authority to an interest rate risk in connection with the Indexed Inverse Floaters that the Authority cannot economically hedge or have an adverse or possibly adverse effect, for federal income tax purposes, on restrictions on the investment of the proceeds of the 1993 Public Education and Health Facilities Refunding Bonds or the amount of rebate payable to the United States with respect to the 1993 Public Education and Health Facilities Refunding Bonds; and

(d) prior to such Optional Conversion there shall not have occurred the enactment, promulgation, execution or ratification of, or any change in or amendment to, any law, regulation or ruling (or in the applicable or official interpretation of any law, regulation or ruling) as a result of which the Authority shall be in receipt of an opinion of nationally recognized bond counsel to the effect that the conversion of any Indexed Inverse Floater would cause the interest payable on any of the 1993 Public Education and Health Facilities Refunding Bonds to cease to be excludable from gross income for federal income tax purposes.

The Internal Revenue Service has issued proposed regulations, which were published in the Federal Register on December 2, 1992, that may, if adopted in their current form, restrict the right of owners to convert Indexed Inverse Floaters in certain circumstances. The regulations, if adopted, would apply only to conversions occurring 30 days or more after publication of the regulations as final. Under the proposed regulations, significant alterations to any debt instrument may cause it to be treated as a reissued debt instrument for Federal income tax purposes. Although it is not clear, it is possible that the exercise of the option to convert an Indexed Inverse Floater may cause it to be treated as reissued under the proposed regulations. If the converted Indexed Inverse Floater were considered to be reissued, the owners would recognize gain or loss measured by the market value of the converted Indexed Inverse Floater. In addition, if the treatment of the converted Indexed Inverse Floater as a reissued obligation would cause interest on the 1993 Public Education and Health Facilities Refunding Bonds to be includable in gross income for Federal income tax purposes, *e.g.*, if the converted Indexed Inverse Floater had a lower yield than the combined yield on the 1993 Public Education and Health Facilities Refunding Bonds and on the 1993 Revenue Refunding Bonds or if there were a change in law adversely affecting the reissuance of the 1993 Public Education and Health Facilities Refunding Bonds, the conversion would not be permitted.

The Authority and GDB have agreed, pursuant to the Master Agreement, to terminate the Rate Swap Transaction in a notional amount corresponding to the face amount of the Indexed Inverse Floaters being converted. Any such termination of such portion of each such Rate Swap Transaction is expressly conditioned on the following:

(a) GDB is actively involved in the business of executing interest rate swap transactions on the basis of tax-exempt market interest rates;

(b) the credit standing of the Authority in the view of GDB has not materially deteriorated from its credit standing on the date that such Rate Swap Transaction was entered into;

(c) GDB arranges, in light of then current market conditions, terms for such termination financially and otherwise acceptable to the Authority and GDB, and the Authority consents to such terms, which consent shall not be unreasonably withheld; and

(d) such other factors as affect GDB's willingness to enter into Rate Swap Transactions.

There can be no assurance that any substitute master agreement will contain the same conditions as the Master Agreement.

In addition, prospective owners of Indexed Inverse Floaters should note that:

(i) pursuant in the Master Agreement. GDB and the Authority have agreed that if the conditions specified above with respect to adjustment of the Rate Swap Transaction are satisfied, they will arrange for such adjustment on a best efforts basis;

(ii) although the Interest Rate Adjustment applicable upon an optional conversion of any Indexed Inverse Floaters to the applicable Converted Rate cannot be determined at this time, such adjustment could, under certain market conditions described above, be substantial; and

(iii) neither the Authority nor GDB shall be responsible for paying the Interest Rate Adjustment to an owner of an Indexed Inverse Floater in the event that a conversion of any such Indexed Inverse Floater on any Optional Conversion Date does not occur for any reason.

The Authority has agreed in the resolution authorizing the 1993 Public Education and Health Facilities Refunding Bonds that it will not terminate a Rate Swap Transaction early or allow GDB to terminate such Transaction early, other than (i) in the case of GDB, upon its rights pursuant to the Master Agreement or (ii) upon an optional conversion of the Indexed Inverse Floaters, unless the Authority shall have received an opinion of counsel nationally recognized on the subject of municipal bonds to the effect that such termination will not cause interest on the 1993 Public Education and Health Facilities Refunding Bonds to be includable in gross income for federal income tax purposes.

*Termination or Substitution of Rate Swap Transactions.* If any Rate Swap Transaction is terminated early or if GDB is in default under the terms of the Master Agreement, the Authority will make reasonable efforts (as set forth in said resolution) to obtain and implement a substitute rate swap agreement as promptly as practicable. If the Authority cannot substitute such agreement at a cost that will not exceed the termination payment to be received by the Authority as a result of the early termination of the prior Rate Swap Transaction, the Authority shall as promptly as practicable either (i) replace the Master Agreement with a more expensive substitute agreement or (ii) elect not to replace it. If the cost of any substitute agreement is less than the cost of the prior Rate Swap Transaction, the Authority may keep the difference provided that, within thirty (30) days of the receipt of such payment, it shall have received an opinion of counsel nationally recognized on the subject of municipal bonds to the effect that such retainage will not cause interest on the 1993 Public Education and Health Facilities Refunding Bonds to be includable in gross income for federal income tax purposes. If the Authority cannot obtain such opinion, then it may seek a private letter ruling from the Internal Revenue Service to the effect that such retainage will not cause interest on the 1993 Public Education and Health Facilities Refunding Bonds to be includable in gross income for federal income tax purposes. If such ruling cannot be obtained within one (1) year of the receipt of such payment, or if the Authority does not seek such private letter ruling, then it shall pay to the holders of the Indexed Inverse Floaters, on the Interest Payment Date next succeeding the earlier of (i) the date on which the Authority elected not to seek such private letter ruling and (ii) the date that is one (1) year after the receipt of the termination payment, the amount of any such savings, together with any investment earnings thereon.

If the Authority elects not to replace the Master Agreement, any termination payment received by it, together with any investment earnings thereon, shall be transferred to a subaccount in the 1978 Bond Service Account and shall be used to pay interest on any Indexed Inverse Floaters to the extent the Indexed Inverse Floaters Rate exceeds the Base Rate at any time after the termination of the Master Agreement. On the Scheduled Conversion Date, the Authority shall be entitled to keep any portion of the termination payment or the investment earnings thereon in such subaccount, provided that the Authority shall have received an opinion of counsel nationally recognized on the subject of municipal bonds or a private letter ruling from the Internal Revenue Service to the effect that such retainage will not cause interest on the 1993 Public Education and Health Facilities Refunding Bonds to be includable in gross income for federal income tax purposes. If the Authority shall have not obtained such opinion or private letter ruling, any such moneys or investment earnings thereon, shall be paid to the holders of the Indexed Inverse Floaters, as interest, on the Scheduled Conversion Date.

***Other Special Considerations.*** **Prospective owners of the Indexed Inverse Floaters should note that the prices at which leveraged instruments, such as the Indexed Inverse Floaters prior to the applicable Conversion Date, may trade in the secondary markets can be expected to fluctuate more in relation to general changes in the interest rates for long-term fixed rate securities than prices of conventional interest bearing securities of comparable maturities. Thus increases or decreases in the general level of interest rates can be expected to result in greater movements in the prices of Indexed Inverse Floaters than in the prices of conventional securities.**

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**CONTENTS**



$713,480,000

Puerto Rico Public Buildings Authority

Consisting of

$128,895,000 Revenue Refunding Bonds, Series L

$584,585,000 Public Education and Health Facilities Refunding Bonds, Series M

Guaranteed by the Commonwealth of Puerto Rico

*OFFICIAL STATEMENT*

**The First Boston Corporation**

**Lazard Frères & Co.**

**Lehman Brothers**

**PaineWebber Incorporated**

**Bear, Stearns & Co. Inc.**

**Donaldson, Lufkin & Jenrette**
**Securities Corporation**

**Goldman, Sachs & Co.**

**Kidder, Peabody & Co.**
**Incorporated**

**Merrill Lynch & Co.**

**Smith Barney, Harris Upham & Co.**
**Incorporated**

**Dean Witter Reynolds**